

ALASKA PERMANENT FUND CORPORATION Annual Report

1999

*Ending the Century:*

Professionalism.

Performance.

Permanence.



## The Alaska Permanent Fund

### A PUBLIC TRUST INVESTING FOR ALASKA'S FUTURE

**T**he Alaska Permanent Fund is an investment savings account that belongs to the State of Alaska. It was created in 1976 by a voter-approved amendment to the Alaska Constitution. The Fund is established as a public trust. This means that the principal of the Fund is to be invested in perpetuity. The beneficiaries of the trust are all present and future generations of Alaskans.

The Permanent Fund is made up of two parts: principal and income. The principal is invested permanently and cannot be spent without amending the state constitution with a majority vote of the people. Decisions about uses of the earnings are made each year by the people's elected representatives – the Alaska State Legislature and the Governor.

The Fund is managed by the Alaska Permanent Fund Corporation (APFC). Policy is established by a six-person Board of Trustees, which has adopted the following investment philosophy:

**Risk Posture.** The Board's overriding investment objective for the Fund is to maintain the safety of principal while maximizing total return. Therefore, it will always act to ensure that the level of investment risk in the Fund is prudent and does not jeopardize that primary objective.

**Return.** The Board believes that over the long term, there exists a relationship between the level of investment risk taken and the rate of investment return realized. It believes that the assumption of a moderate level of risk is reasonable and justified in order to enhance potential long-term returns, understanding that it will produce a wider range of expected returns than more conservative asset mixes. This range of expected returns will narrow as the investment time horizon is lengthened, which fits well with the Fund's role as a long-term investor.

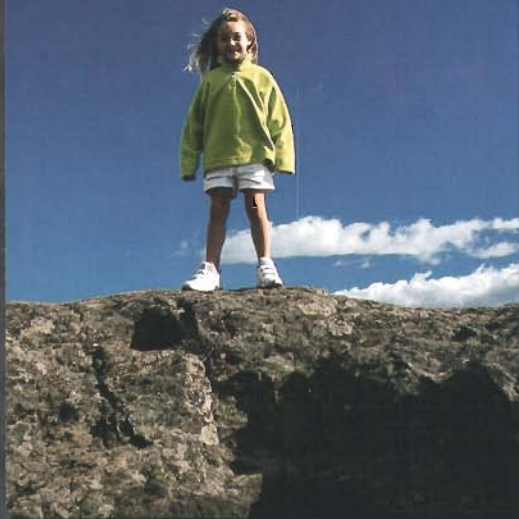
**Diversification.** The primary technique employed by the Board to reduce risk and enhance returns is diversification.

**Liquidity.** The Permanent Fund is managed with a long-term investment horizon, but seeks to avoid major fluctuations in year-to-year results. Although major consideration is given to capital growth over the long term, appropriate consideration is given to current income. This meets the statutory requirement to provide benefits for both current and future generations of Alaskans.

#### Contents

About this Report .....	1
Report to Alaskans .....	2
Professionalism .....	6
Performance .....	12
Permanence .....	20
Auditors' Report .....	25
Financial Statements .....	26

## About this annual report



As Alaskans prepare to celebrate a new decade and a new century, it is appropriate to take a look back at the qualities that made the Alaska Permanent Fund the state's largest asset.

**Professionalism. Performance. Permanence.**

**Professionalism** entails the day-to-day activities of the Fund – the hundreds of big and little decisions that collectively define how the Alaska Permanent Fund Corporation (APFC) staff and Trustees conduct their business as the stewards of the Fund. **Performance** takes a longer perspective and measures the effectiveness of balancing risk and opportunity, adding value through strategic planning and doing business in a professional manner. **Permanence** is the strategic goal – a strong focus on professionalism and performance to guarantee that the Fund will continue to benefit current and future generations of Alaskans for all of the future.

The importance of the three values was summarized by former Trustee Lee E. Fisher who wrote: “The yellow gold that marked Alaska’s entry into the 20th century has been replaced by Permanent Fund investment gold marking Alaska’s entry into the 21st century. By virtue of the professionalism of Trustees and staff, the continuing exemplary performance of the Fund assures permanence for future generations.”

# Report to Alaskans

**T**he Alaska Permanent Fund ended the final year of the decade with a balance of \$26.4 billion and investment earnings more than double state oil revenues.

It was just a year ago that Fund earnings became the state's largest source of income. With oil production and revenues at 20-year lows, the interest earned on the Fund's bond portfolio alone equaled all the oil royalties and severance taxes that flowed into the state's general fund.

As the administration and state legislature grappled with a \$1 billion budget deficit, Alaska's elected officials demonstrated their confidence in the Fund by granting the APFC increased investment flexibility. That legislation will help the Fund earn substantial additional amounts in future years.

The legislature and administration also asked Alaskans' advice on future uses of Fund income.

The Fund finished the year with its first-ever \$1 billion transfer for the payment of 1999 dividends.

## **A good year for the Fund**

While fiscal 1999 was a year of consolidation and retrenchment for many of Alaska's core businesses, it was a good year for the Fund. Spurred by a strong domestic equities market, the Fund increased its value to Alaskans by \$1.4 billion, net of the 1998 dividend transfer of \$893 million.

The Fund earned \$2.5 billion of statutory net income, more than half of which came from realized stock gains. In addition, the Fund ended the year with \$3.7 billion of unrealized gains. That means the stock portfolio's market value of \$13.1 billion could drop more than one-fourth and still be worth more than its cost.

## **Fund earns 9.49 percent**

The Fund earned a 9.49 percent total return, its overall performance dampened by having more than 40 percent of its assets invested in bonds, which experienced a 1.68 percent return for the year. Domestic bonds experienced their worst year in five years. Nonetheless, with inflation at a mild 1.54 percent, the Fund's real rate of return was 7.95 percent, almost double the Trustees' long-term annual growth target of 4 percent above inflation.

## Another wild ride in the stock markets

The domestic equities market remained strong but volatile during the year, rallying from a major decline in the first quarter that was driven by uncertainty in emerging markets, primarily Russia. The S&P 500 ended the year up a vigorous 22.76 percent, its fifth consecutive year of 20-plus percent returns. The broader Russell 3000 Stock Index experienced a 20.09 percent return. The APFC domestic stock portfolio had an excellent year, returning 19.37 percent.

The recovery in the Asian and Japanese markets that began during the second quarter grew stronger as the year progressed, offsetting weak European markets. The MSCI EAFE (Morgan Stanley Capital International Europe, Australia and Far East) Index posted a total return of 7.62 percent. Compared to this benchmark, the APFC's non-U.S. stock portfolio turned in an above-average year, returning 9.40 percent. Capital Guardian Trust Co. achieved the best performance, beating its benchmark by 16 percentage points.

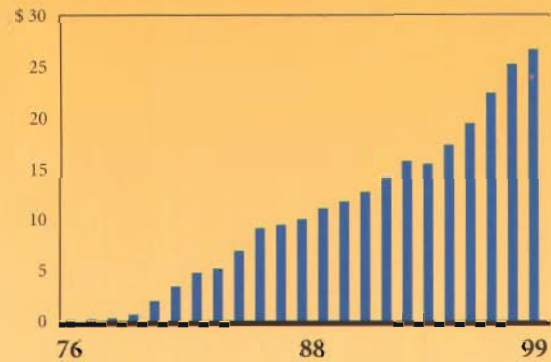
After losing more than 50 percent of its value last year, emerging markets rebounded, with the MSCI Emerging Markets Global Index returning 33.52 percent. The APFC funded two new emerging markets accounts during the fourth quarter, transferring \$250 million each to Capital Guardian and Schroder Investment Management North America. Capital Guardian also received \$300 million in funding for a new Small-Cap U.S. portfolio.

## Poor year for fixed income

Following a strong first quarter, the Fund's U.S. fixed-income portfolio declined in value, producing a composite return of 1.68 percent. The same factors that contributed to the prior year's strong results detracted from this year's performance. Most notably, the composite portfolio had greater-than-market

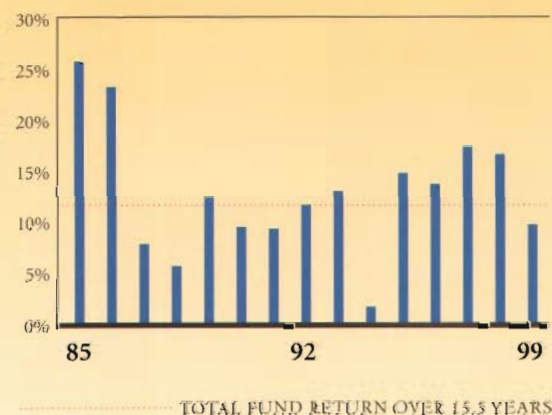
## Growth of Fund Since Inception

(DOLLARS IN BILLIONS, AT MARKET VALUE)



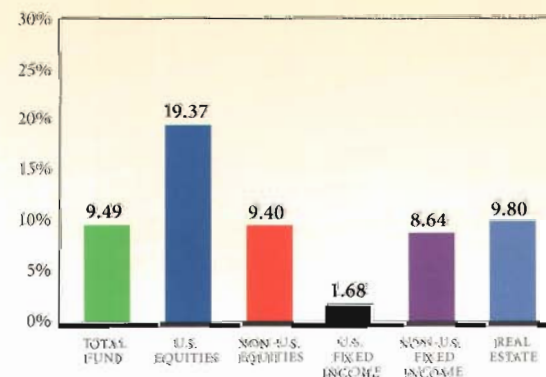
## Permanent Fund's Total Return

(BY FISCAL YEAR)



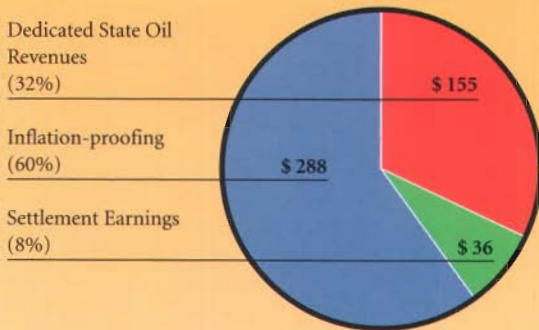
## Total Rate of Return

(FISCAL 1999)



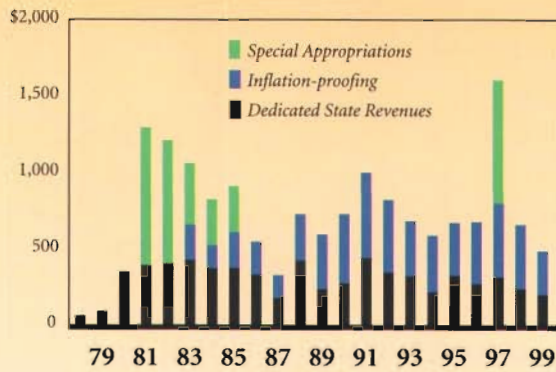
### Additions to Principal

(FISCAL 1999 IN MILLIONS)



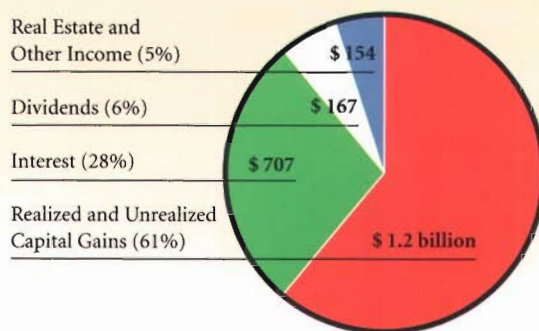
### Contributions to Principal

(SINCE INCEPTION, DOLLARS IN MILLIONS)



### Sources of Net Income

(IN MILLIONS)



interest rate sensitivity (duration). All but one of the portfolio's managers lagged their benchmark. Sanford Bernstein's defensive outlook supported that firm's comparatively strong 4.03 percent full-year result.

Both of the Fund's international bond managers produced solid returns, well outperforming their benchmark.

### Real estate returns 9.8 percent

The APFC diversified its real estate holdings by adding a mortgage portfolio that includes investment-grade public and private mortgages, and by fully funding the REIT (Real Estate Investment Trust) portfolio. In direct investments, the Corporation sold 17 properties during the year, purchased two and increased its ownership in 10. The portfolio returned 9.80 percent during the year, two percentage points ahead of its benchmark.

### Legislature moves to increase Fund investment flexibility

At the request of the Board of Trustees, the legislature passed and the governor signed, a bill that raises the limit on equity investments from 50 percent to 55 percent. The legislation also allows Trustees to invest a further 5 percent of Fund assets to: (1) make or retain greater asset class commitments than currently allowed; and/or (2) invest in individual securities or instruments that are not expressly permitted. These new investments must satisfy the prudent investor rule.

The new investment flexibility will increase the Fund's return by permitting an expansion of its stock portfolio and allowing managers to add incremental value. Equities have significantly outperformed all other asset classes over the long term.

The Trustees revised the Fund's asset allocation in June to allow equities to rise to 52 percent while they consider additional changes to improve investment performance in the next century.

Governor Tony Knowles appointed Natural Resources Commissioner John Shively to the Board, replacing Mark Boyer who left the administration during the year.

As we end the century, we asked former Trustees to reflect back on the 23 years of the Fund's existence. Observations are included throughout the report. Here are the comments of John Kelsey, the longest-serving Trustee:

"The Alaska Permanent Fund is a dream come true for all Alaskans that is the result of foresight and taking a professional approach to investment management. The performance of this truly unique organization has been outstanding and should continue to produce great wealth for generations to come."



Eric E. Wohlforth  
Chair, Board of Trustees



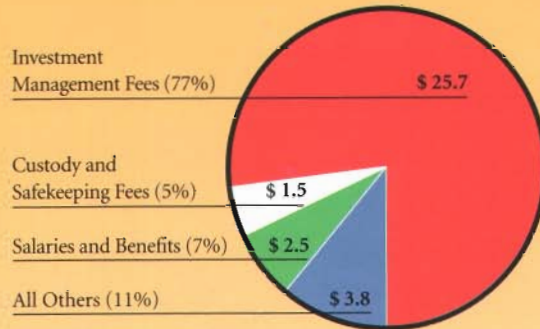
Byron I. Mallott  
Executive Director



APFC BOARD OF TRUSTEES & EXECUTIVE DIRECTOR  
From left, rear: Executive Director Byron I. Mallott, Trustee Wilson L. Condon, Trustee Jim Sampson, Trustee John Shively.  
Front row: Trustee Melphine Evans, Chair Eric E. Wohlforth, Vice Chair Clark S. Gruening.

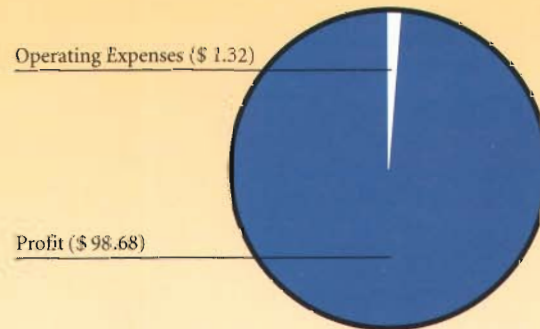
### Corporation Expenses

(IN MILLIONS)



### Expense Ratio

(PER \$ 100 OF FUND STATUTORY INCOME)

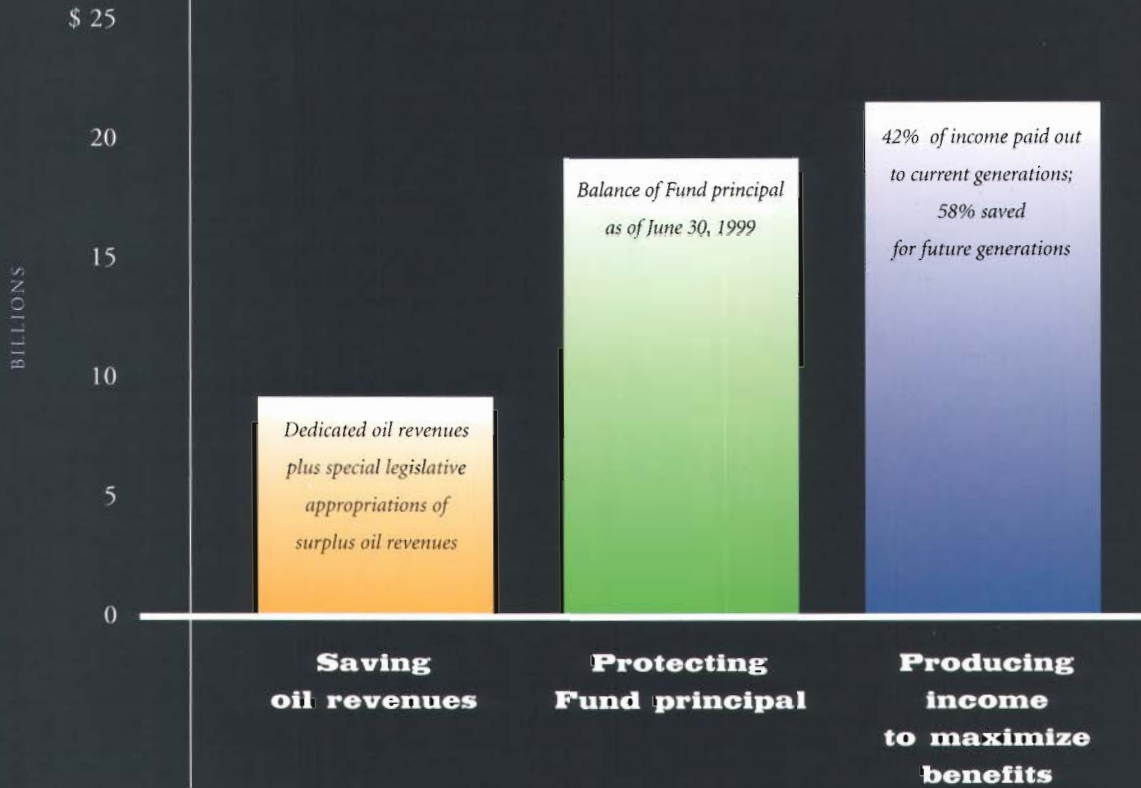


### Other Alaska Funds Under APFC Management

(YEARS ENDED JUNE 30)

	1999	1998
Alaska Science and Technology Foundation	\$ 124,887,000	129,092,000
Alaska Mental Health Trust Fund	305,939,000	299,356,000
International Trade and Business Endowment Fund	5,927,000	5,710,000

**The Alaska Permanent Fund is achieving its goals**



# Professi

Technology (photo at far right) has enabled the APFC to grow the Fund to \$26.4 billion of global assets and earn a 12.02 percent rate of return over the past 15.5 years with a small staff and one of the lowest expense ratios of any institutional investor in the world. The return has benefited both current and future generations of Alaskans, as the chart above illustrates. In photo at right, Randy Sears (left), the APFC's Manager of Fixed Income, helps manage \$9 billion of bonds internally from a trading desk staffed by three. To his right is Peter Naoroz, Manager of the Fund's \$2.1 billion real estate portfolio.

*The knowledge and experience that allows the right investment tools to be applied in the right combination ...*



## Professionalism

“Professionalism,” said former Trustee Tom Williams, “is the knowledge and experience that allows the right investment tools to be applied in the right combination so as to achieve optimal performance over the long run. Without it, the chances of achieving that performance are virtually nil.”

Professionalism is a dynamic concept – a process that began with public expectations when the Corporation was established, the policies it follows, the technology it utilizes, the relationships it builds with its managers and the excellence of its operations.

## Separation without isolation

It took four long years of debate and hearings before SB 161 passed in 1980, establishing the APFC and firmly insulating it from politics, while maintaining its public accountability. It was a bitter battle at times. Some wanted to keep the Fund as an arm of the administration. Others raised concerns that



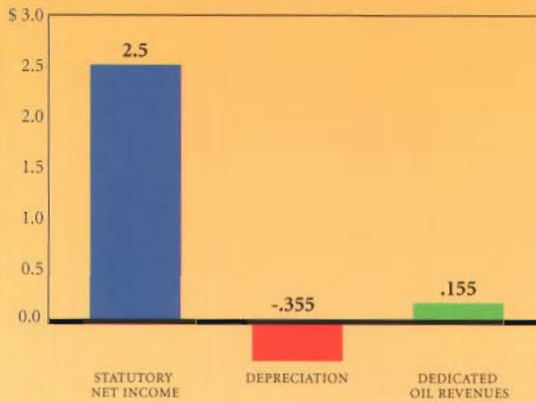
### **The mission** of the Alaska Permanent Fund

Corporation is to maximize the value of Alaska's oil revenues through prudent long-term investment and protection of principal to produce income to benefit all current and future generations of Alaskans.

# Professionalism

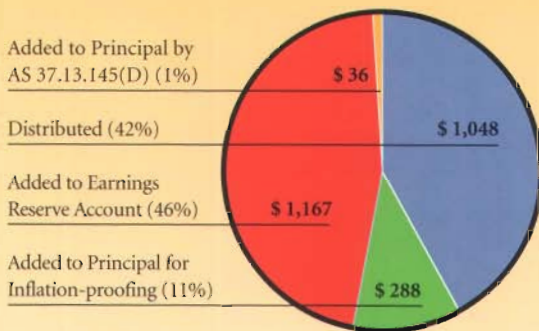
### Sources of Growth

(FISCAL 1999, DOLLARS IN BILLIONS)



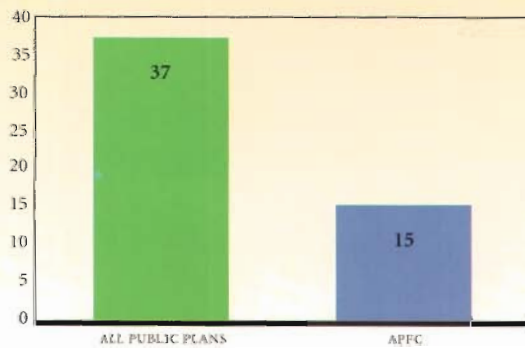
### Uses of Statutory Net Income

(IN MILLIONS)



### Average Management Costs

(COSTS EXPRESSED IN BASIS POINTS)



100 basis points = 1%

Figures according to 1998 Survey by Greenwich Research Associates

Alaska was creating a “political monster,” capable of creating millionaires “to the detriment of the general welfare of Alaska.”

But ordinary Alaskans were firm in their desire to keep the Fund and its day-to-day operations separate from the political process. And they prevailed. The legislature achieved political neutrality through the creation of an independent corporation firmly focused on investment decisions, managed by a board of trustees. To ensure accountability, the legislature retained control over the Corporation’s budget and list of authorized investments.

“By restricting the duties of the Trustees to investment management, their task was simplified, their performance could be objectively measured in the marketplace and they were freed in large measure from social and political pressures,” said Elmer Rasmuson, who was the Trustees’ first chairman.

“In truth, much of the success and prestige of the Permanent Fund is due to their singleness of financial stewardship. The contrast with the early performance of the Alberta Heritage Fund is eloquent proof of the superiority of the Alaska course of action.”

### Institutionalizing checks and balances

When Dave Rose was appointed the APFC’s first executive director in 1982, he had a staff of one, \$4.6 billion of assets to manage and a short investment list. Today, the APFC has a staff of 31 and \$26.4 billion of assets invested in stocks and bonds in 44 countries, along with 62 commercial properties located in the U.S. It manages about \$9 billion of fixed-income internally, from a trading desk staffed by three, and supervises the activities of five external fixed-income managers.

One investment officer oversees the 11 equities managers who collectively manage portfolios worth

\$13 billion. The four-person real estate section travels extensively, inspecting the Fund's \$2 billion real estate holdings and monitoring the performance of 15 external managers. The chief investment officer directs all these activities.

Each day, millions of Fund dollars change hands as these 30 managers and the in-house staff buy and sell different investments. All these transactions flow through the custodian bank, which reconciles the transactions and holds the securities in trust for the Corporation.

It's a complicated process made safer by standardized manager contracts and policies and strict due diligence processes, all monitored by staff and third-party contractors.

"Alaskans should all be thankful that, from the very beginning, the Alaska Permanent Fund Corporation has always enjoyed professional investment staff and managers of the highest caliber, and it continues to enjoy this today," says former Trustee Tom Williams.

### **Using technology to keep in touch**

"As we move from the Industrial Century into the Information Century, the Alaska Permanent Fund is well positioned to take full advantage of the technology to succeed in the New Millennium," said former Board Chairman Carl F. Brady, Jr.

Technology has allowed the Corporation to manage \$26 billion of global assets with a minimal staff and one of the lowest expense ratios of any institutional investor in the world. It has improved performance, kept costs down and increased due diligence.

The heart of the Corporation's technology is its Management Information System (MIS), which underwent a complete metamorphosis starting in 1995. Today, the MIS provides real-time, daily pricing of securities, enabling staff to better monitor trades and track manager performance. Part of the system is linked to the Corporation's website to allow Alaskans to monitor the Fund on a daily basis.



### *Greeting the new century with confidence*

Five years ago, the APFC realized it had a bug in its system, the Millennium Bug, which could insert errors into thousands of pages of critical documentation and endanger millions of dollars of transactions as Alaska greeted the year 2000.

In the time since, the APFC has taken all necessary precautions to ensure that the Fund's investments will be fully protected when the clock strikes the magical hour.

The Corporation's efforts began back in mid-1994 when it started to replace critical computer programs, such as its Management Information System that provides real-time investment information and accounting data. These are now fully compliant, with backup and redundancy procedures in place.

The Corporation worked with its custodian bank to create a back-up set of books as an added safeguard against system failure. It required all of its managers to certify that their systems are Y2K compliant.

With the clock ticking, the biggest challenge now is emerging nations, which may not be as fully prepared as developed countries. The APFC's non-U.S. managers have notified the APFC that they intend to closely monitor the situation, and they will stop trading in markets where they perceive Y2K risk to be sufficiently high to warrant greater precautions.



Jim Patterson, Executive Vice President, CB Richard Ellis Investors

## *Adding value through better communications*

When the APFC met collectively with its external managers last fall, it asked them to offer concrete suggestions on how to add incremental value to the Fund's performance.

There were lots of suggestions and many of them were incorporated in HB 156, which increased investment flexibility for the Corporation. Some of the most creative ideas came from the real estate managers, including CB Richard Ellis Investors, which manages \$291 million of assets for the Fund.

"These enhanced capabilities will permit a much more flexible approach to satisfying the expansion needs of tenants whose space requirements cannot be adequately met through the availability of space in existing Fund assets by the ability to acquire additional land on which to expand or add to existing facilities," said Managing Director James Patterson.

"Advisors can also explore the benefits of adding leverage to existing Fund assets that are currently debt-free. The resulting loan proceeds can be returned to the Fund to improve returns in the short run or may be reinvested in existing assets to upgrade or refurbish the properties thereby maintaining competitiveness and adding value in the longer term."

The internal accounting portion of the MIS was replaced in 1998 so that it conforms to new national standards and produces financial reports much faster. The update improved communications with the Corporation's custodian bank, the Bank of New York, which has led to better money management and improved due diligence.

The board room was updated to include a modern videoconferencing facility. This has improved communications between staff and external managers and made it easier for Alaskans to participate in board meetings.

The updates have also brought the Corporation into Y2K compliance.

## **Strong relationships bring better performance**

Last fall the Corporation asked all of its managers to gather in New York to discuss overall market conditions and strategy and to suggest ways to improve performance and add incremental value. It was a good beginning, and one that will be repeated as part of the APFC's annual meeting.

Several of the ideas were incorporated into HB 156, legislation enacted this session that will enable the Fund to increase earnings substantially in the future.

This bill raised the equities ceiling to 55 percent, and enacted a new 5 percent prudent investor category.

In June, the Trustees expanded the investment flexibility of its global equity managers and its two non-domestic fixed-income managers and changed the short-term benchmark for the non-domestic fixed-income managers. The managers will now be able to opportunistically buy investments outside their benchmarks, within limits, if the purchases will add value and diversify risk.

## Composition of Non-U.S. Equity Portfolio by Country

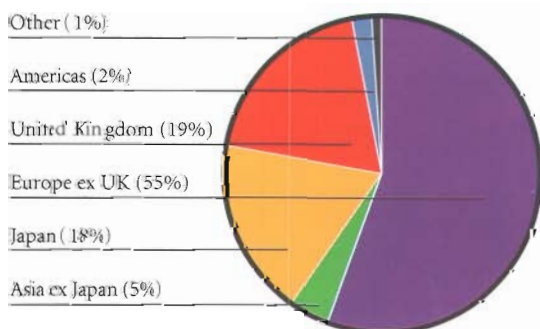
(DOLLARS IN MILLIONS)

	MARKET VALUE	% OF TOTAL	UNREALIZED GAIN/(LOSS)
Argentina	\$ 9.4	0.2	(0.4)
Australia	157.0	3.9	35.2
Austria	3.7	0.1	0.2
Belgium	32.6	0.8	3.2
Botswana	2.0	0.0	0.0
Brazil	33.0	0.8	(0.7)
British Virgin Island	41.5	1.0	(0.3)
Canada	32.6	0.8	7.4
Chile	5.4	0.1	0.3
Denmark	26.0	0.6	3.3
European Union	15.3	0.4	4.9
Finland	88.4	2.2	42.5
France	361.3	8.9	86.6
Germany	418.4	10.3	105.8
Greece	13.5	0.3	(1.5)
Hong Kong	87.2	2.2	19.1
Hungary	6.7	0.2	(0.2)
India	7.9	0.2	1.0
Indonesia	9.9	0.2	0.2
Ireland	7.9	0.2	1.4
Israel	9.1	0.2	0.0
Italy	126.1	3.1	39.8
Japan	709.5	17.5	44.1
Korea	57.7	1.4	19.5
Malaysia	22.3	0.6	(6.3)
Mauritius	0.2	0.0	0.0
Mexico	57.7	1.4	19.5
Netherlands	198.0	4.9	37.0
New Zealand	8.8	0.2	(1.7)
Norway	2.9	0.5	(0.6)
Philippines	19.0	0.5	0.0
Poland	1.6	0.0	0.2
Portugal	7.5	0.2	(0.5)
Russia	1.1	0.0	0.2
Singapore	59.1	1.5	10.5
South Africa	39.9	1.0	3.8
Spain	87.6	2.2	22.8
Sweden	93.1	2.3	26.8
Switzerland	218.8	5.4	41.5
Taiwan	1.7	0.0	0.4
Thailand	8.3	0.2	0.3
Turkey	19.0	0.5	(1.6)
United Kingdom	720.8	17.8	131.2
United States *	196.0	4.8	21.3
<b>Total</b>	<b>\$ 3,663.4</b>	<b>100%</b>	<b>\$ 664.7</b>

\* American Depository Receipts (ADRs) purchased by non-U.S. managers

## Non-U.S. Equities

(BY REGION)



Trading room at Dresdner RCM, a growth equities manager.

## Keeping investments fully working

In an effort to increase long-term performance, Trustees directed the Fund's equity managers to be fully invested at all times by reducing their cash reserves to no more than 2 percent.

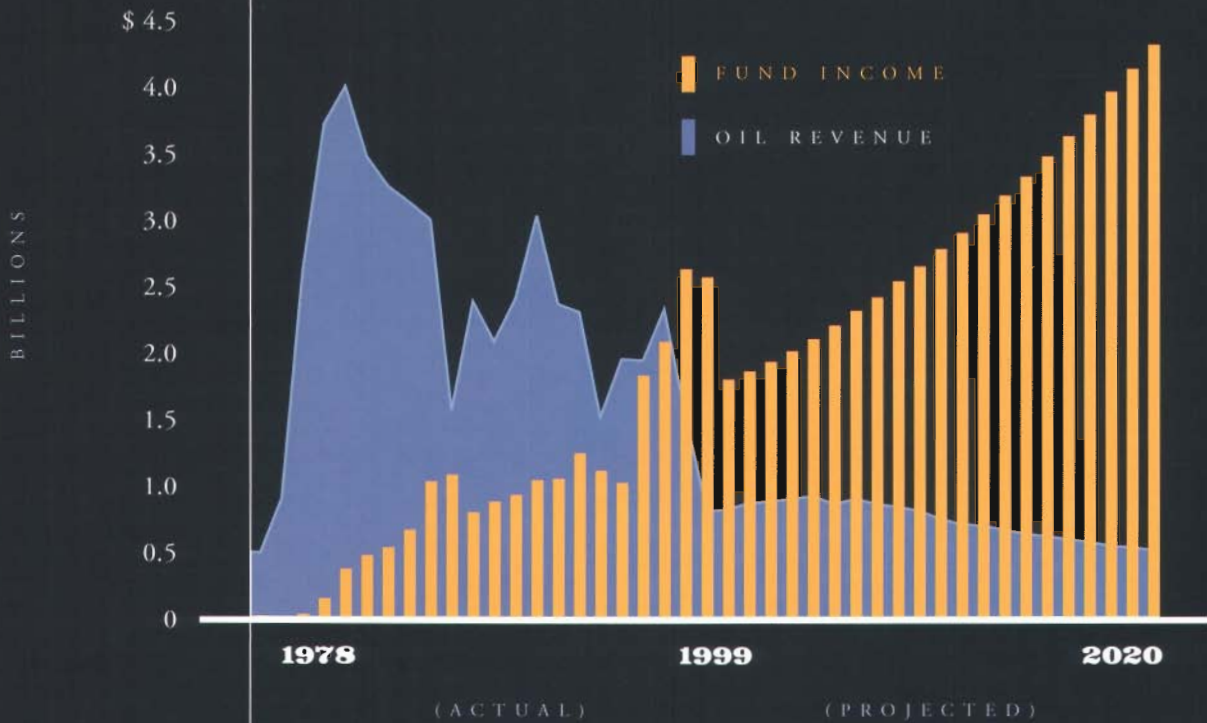
Managers sometimes use cash as a tactical and strategic investment tool and have been allowed to hold up to 15 percent of their portfolios in cash before notifying the APFC of their intent to hold a greater amount of cash.

Cash has historically returned only a fraction of equities performance and can reduce long-term overall performance.

The APFC changed its policy after surveying its managers and other institutional investors. It found most managers agreed that a fully invested portfolio would not detract from performance and that most other public institutions defined "fully invested" as less than 5 percent in cash.

The new policy includes control bands that range from 0 percent to 5 percent to provide latitude to accommodate management styles and market conditions. Additionally, managers may elect to exceed 2 percent cash for a period of 90 days or hold cash greater than 5 percent if their strategy indicates it would be beneficial to the APFC. Managers must notify the Corporation prior to implementing such a strategy and will be placed on review status.

**Permanent Fund Statutory Net Income  
vs. State Oil Revenue**

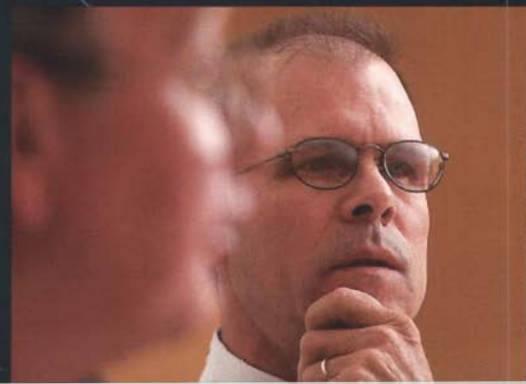


# Perfor

Driven by a strong domestic equities market, the Fund has become the state's largest asset, producing more state revenues than oil, as the chart above shows.

The projections for the years 2000-2020 are based on Department of Revenue's forecast for future oil prices and the APFC's forecast for future Fund earnings. APFC Chief Investment Officer Terry A. Brown, right, speaks with Michael O'Leary of Callan Associates, the Corporation's performance analyst, while the New York Stock Exchange, at far right, wraps up another busy day.

*Fund earnings have become Alaska's largest source of income for the future.*



## Performance

Equities and globalization – the two most defining concepts for a \$26.4 billion Fund prepared to enter the 21st Century.

It was a transformation that came gradually. When Dave Rose took over as the APFC's first executive director, the Fund was entirely invested in fixed-income instruments, and the APFC was prohibited from entering the global equities markets.

The early restrictions hurt the Fund, said Elmer Rasmuson, the Trustees' first chairman. The initial stock allocation was too small and the legislature's hesitancy to allow equity investment outside the United States cost Alaska "multi-million dollars in lost income," Rasmuson said.

But Alaska was new at the investment business and as it grew more confident, it began to expand its investments. The Fund bought its first stocks in 1983.

## Emerging nations – a new frontier

In an effort to boost performance and gain greater diversification, the APFC funded two new emerging markets accounts and provided increased flexibility for the global managers to take advantage of opportunities in emerging markets.

Emerging markets returned a robust 33.52 percent during the fiscal year and a 4.73 percent return over the past 10 years.

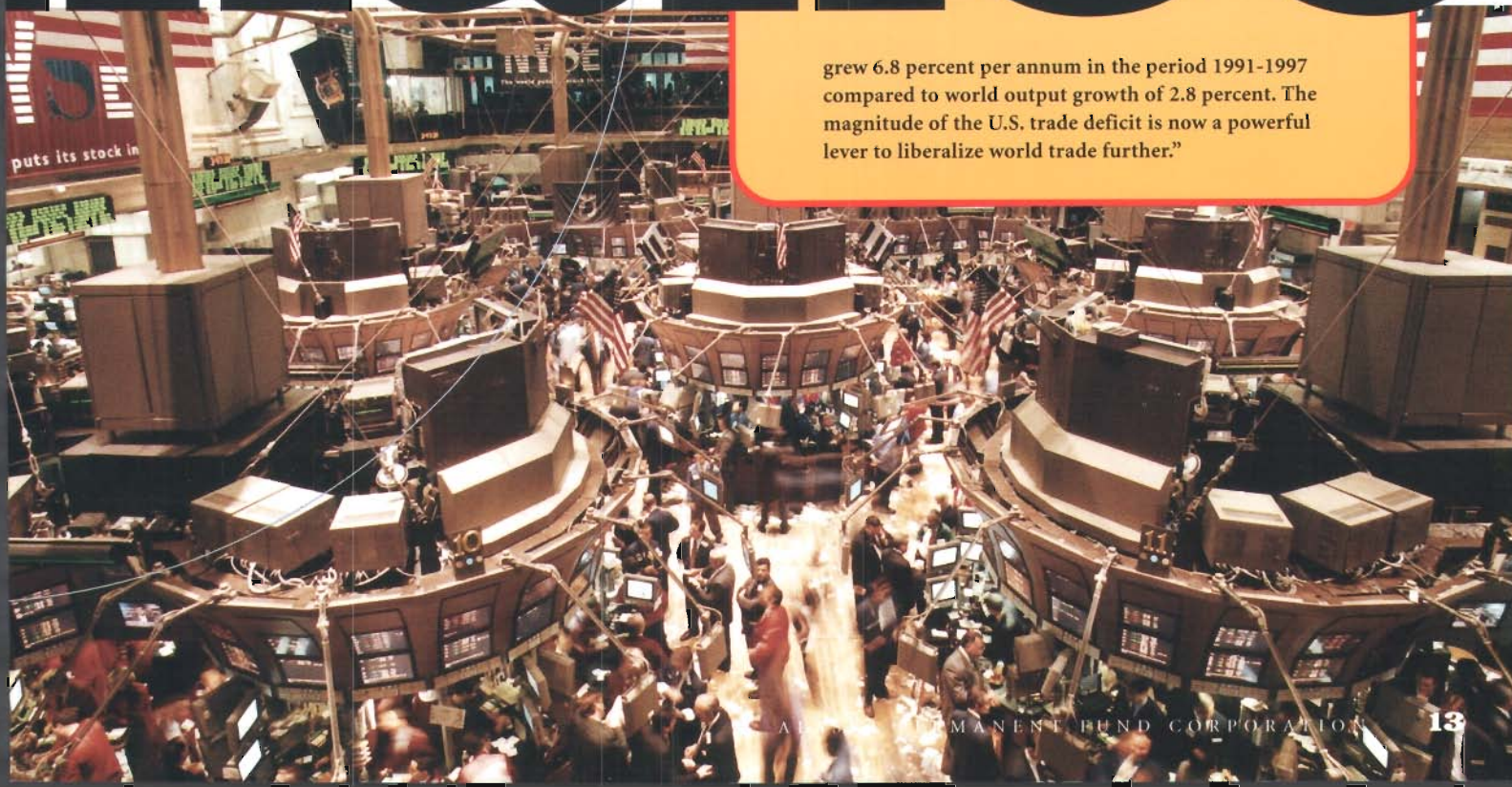
While the economies of individual countries can be capricious, a well-diversified emerging markets portfolio can reduce overall volatility because the countries are not correlated with each other or with other asset classes, such as the EAFE Index or the S&P.

Fund managers believe that many of these countries are maturing, which will reduce risk over the long-term. Rogge notes that the collapse of the Soviet system forced these economies to become increasingly dependent on international capital markets, which pushes them towards Western capitalism. Democratic processes have made advances in many of the countries, and incomes have become more equal in Asia, the Middle East, North Africa and Latin America.

Emerging markets' economies are primarily exporters, Rogge says, "and are therefore exposed to the faster growth of trade than output. World trade volumes

# performance

grew 6.8 percent per annum in the period 1991-1997 compared to world output growth of 2.8 percent. The magnitude of the U.S. trade deficit is now a powerful lever to liberalize world trade further."



## Domestic Equities Managers' Performance

(AS OF JUNE 30, 1999)

MANAGERS	MARKET VALUE (IN MILLIONS)	1-YEAR RETURN	BENCHMARK
Deutsche Asset Mgt. *			
S&P 500	\$ 3,302	22.66%	22.76%
Deutsche Asset Mgt.			
S&P 1000	770	11.62	11.62
Ark Asset	642	12.58	22.76
Brinson Partners	443	15.06	22.76
Capital Guardian Small-Cap	215	NA	NA
Dresdner RCM	1,156	36.18	21.84
Dresdner RCM Small-Cap **	245	-1.92	9.29
INVESCO	581	14.68	22.76
Lazard Frères	657	21.18	22.76
Putnam Investment	907	21.76	22.76
Society Asset	455	-6.12	17.19
<b>Combined Return</b>		<b>19.37</b>	

### BENCHMARK RETURNS

Russell 2000 **	9.29%
S&P 500 Index	22.76
S&P MidCap Index	17.19
80% S&P 500/20% S&P MidCap	21.84
S&P 1000	11.62

\* Deutsche Asset Mgt. was formerly Bankers Trust

\*\* 1/2 year only

## International Equities Managers' Performance

(AS OF JUNE 30, 1999)

MANAGERS	MARKET VALUE (IN MILLIONS)	1-YEAR RETURN	BENCHMARK
Deutsche Asset			
Management EAFE	\$ 1,131	7.93%	7.55%
Brinson Partners	436	6.22	7.55
Capital Guardian	539	23.97	7.55
Capital Guardian Emerging	214	NA	NA
Clay Finlay	714	-4.97	-0.85
Dresdner RCM Global *	144	3.97	3.80
Lazard Frères	482	5.23	7.55
Schroder	203	57.56	60.90
Schroder Emerging	268	NA	NA
<b>Combined Return</b>		<b>9.40</b>	

### BENCHMARK RETURNS

MSCI EAFE Free-U.S. dollars	7.55%
MSCI Europe	-0.85
Pacific ex Japan (Custom)	60.90
MSCI EAFE Free-U.S. dollars *	3.97

\* 1/2 year only

## Adding incremental value

This year, the legislature further expanded investment options, increasing the equity ceiling to 55 percent and additionally allowing Trustees to invest up to 5 percent of the Fund's assets in discretionary investments. The legislation also allows the APFC to build new properties in locations where it already owns real estate, removes the \$150 million cap on wholly-owned properties, enables the Corporation to use non-resource debt to increase yield, lets it commit to purchasing a building under construction and expands allowable investments to include real estate operating companies.

These changes bring the Fund into parity with other institutional investors, and also allow Fund managers to add incremental value with 5 percent of Fund assets through such investments as future contracts, equity index futures, enhanced S&P 500 Index strategies, equipment trust certificates, asset-backed securities, private equity and debt securities, U.S. high-yield securities and emerging markets debt, bonds and currency.

Trustees and staff will spend the next six months analyzing these new options and preparing recommendations for the Spring 2000 Asset Allocation Resolution. In June, Trustees allowed the equities ceiling to rise as high as 52 percent.

## Equities produce highest returns over the long term

The formation of the Fund coincided with the longest bull market in history. Over the last 15.5 years, the Fund's domestic equities portfolio returned 17.34 percent, compared to 9.57 percent for domestic fixed income and 8.74 percent for real estate. Note: equities and fixed-income investments are gross of fees; real estate is net.

Trustees have capitalized on this strong growth by increasing equity allocation to the maximum allowed by statute, entering the international stock markets in 1990 and allocating nearly 40 percent of the equity investments to passive management. Stock indexing reduces management fees and produces attractive returns during rising markets. Over the past 15.5 years, only Dresdner RCM, a domestic growth manager, has exceeded the Deutsche Asset Management's S&P 500 returns. Today, the APFC has about \$5.2 billion in portfolios indexed to the S&P 500, S&P 1000 and MSCI EAFE indexes.

### Diversification through segmentation

With the Fund's equities portfolio at \$13.1 billion, the Trustees have moved to protect investments through diversification. Domestic equities comprise 72 percent of the stock portfolio, divided between growth and value portfolios, active and passive management. Trustees decided to seek a new Large-Cap U.S. aggressive growth manager to improve performance. The manager will be selected in fiscal 2000.

During fiscal 1999, growth managers tended to outperform value managers as the equity markets performed well against a backdrop of good but not overheated economic growth, good corporate profit levels and earnings results, a favorable interest rate environment and strong purchase flows by retail investors into mutual funds. The median U.S. growth manager returned 22.63 percent, while the median U.S. value manager returned 13.82 percent. The median Small-Cap U.S. manager had a negative return of -1.12 percent.

### Real Estate Performance

(PERIODS ENDED JUNE 30, 1999)

MANAGERS	RETURN	TARGET BENCHMARK
1-YEAR	9.80%	7.80%
3-YEARS	11.40	11.42
5-YEARS	9.99	10.38
15.5-YEARS	8.74	6.01

### Managers' Performance

(AS OF JUNE 30, 1999)

MANAGERS	MARKET VALUE (IN MILLIONS)	1-YEAR RETURN
AEW Capital Management	\$ 167	25.82%
CB Richard Ellis	291	8.74
Kennedy Associates	284	10.09
L&B Property Advisors	237	9.36
Sentinel	193	9.99
Other managers combined		10.00
Heitman Capital	90	
Henderson Investors	74	
LaSalle Advisors	74	
The RREEF Fund	46	
Raymond James	74	
SSR Realty Advisors	31	
<b>Combined Direct Investment Return</b>		<b>11.24</b>
<b>Commingled Pools</b>	<b>14</b>	<b>16.74</b>
<b>Real Estate Investment</b>		
<b>Trusts (REITs)</b>	<b>462</b>	<b>4.00</b>
AEW Capital Management	411	
Simon Property Group	51	
<b>Real Estate Mortgage and CMBS</b>	<b>124</b>	<b>NA</b>
Lend Lease		
<b>Combined Return</b>		<b>9.80</b>

### BENCHMARK RETURNS

Real Estate Target	7.80
NCREIF Classic	13.60
Morgan Stanley REIT	-8.41
Lehman Brothers Corporate Series A	-2.91

*The APFC target benchmark for real estate securities as of January 1, 1999 consists of 65 percent NCREIF Classic Index, 20 percent Morgan Stanley REIT Index and 15 percent Lehman Brothers Corporate Series A. Excluding AEW REITs, all APFC real estate returns are reported "net of fees."*

## Fixed Income Managers' Performance

(AS OF JUNE 30, 1999)

U.S. MANAGERS	MARKET VALUE (IN MILLIONS)	1-YEAR RETURN	BENCHMARK
APFC In-House	\$ 9,499	1.60%	2.69%
Alaska Permanent Capital Management	150	2.54	3.15
Brinson Partners	200	2.20	3.15
Sanford Bernstein	237	4.03	3.15
<b>Combined Return</b>		<b>1.68</b>	

### BENCHMARK RETURNS

Lehman Brothers Aggregate	3.15%
Lehman Brothers Govt/Corp	2.69

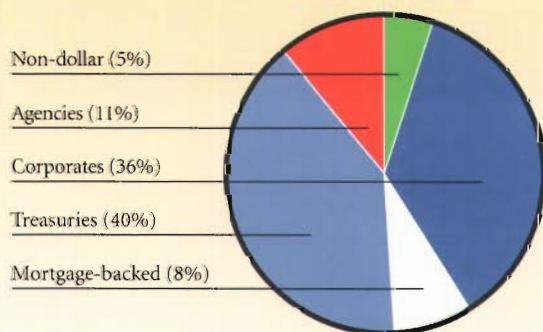
NON-U.S. MANAGERS	MARKET VALUE (IN MILLIONS)	1-YEAR RETURN	BENCHMARK
Julius Baer	\$ 270	7.34%	7.06%
Rogge Global	338	9.65	7.06
<b>Combined Return</b>		<b>8.64</b>	

### BENCHMARK RETURN

Salomon Hedged Non-U.S. Government Bond	7.06
--	------

## Composition of Bonds

(JUNE 30, 1999)



### COMPOSITION OF CORPORATE BONDS

Industrial	11.6%
Banking and Finance	12.0
Utilities	8.3
Yankees	4.2

Dresdner RCM and Putnam, the two domestic growth managers, returned 36.18 percent and 21.76 percent. Returns for the four Large-Cap U.S. value managers were: Ark Asset, 12.58 percent; Brinson Partners, 15.06 percent; INVESCO, 14.68 percent; and Lazard Frères, 21.18 percent. Society Asset, the Mid-Cap U.S. value manager, returned -6.12 percent.

To further diversify holdings and better position the Fund for a possible market shift, the Corporation funded a new \$300 million U.S. Small-Cap portfolio managed by Capital Guardian.

## Asia rebounds as Europe stalls

With \$3.7 billion in non-U.S. dollar stocks, the Corporation has focused increasingly on global management with broader international diversification. Seven managers direct five different types of portfolios, including three specialty ones. The strategy has paid off. The APFC's non-U.S. stock portfolio has collectively exceeded its target benchmark for the last seven years.

In fiscal 1999, the resurgence in Asia and Japan more than offset the weakness in Europe. Clay Finlay, the Corporation's European specialist, returned -4.97 percent, well below its seven-year average return of 16 percent. In contrast, the APFC's Pacific Rim specialist, Schroder, ended the year up 57.56 percent, regaining more than half the prior year's loss of -52.26 percent.

As part of its diversification tactics, the Corporation transferred \$500 million into two new emerging markets portfolios managed by Capital Guardian and Schroder. The transfer had been approved more than a year ago, but was delayed until non-developed international markets recovered. The MSCI Emerging Markets Global Index returned 33.52 percent during the year. Trustees have established a 2 percent allocation to emerging markets equities.

## Steady income producer

Change has come to the Fund's fixed-income portfolio, moving part of it into the global world and bringing new technology into its internal world.

After the legislature increased the Corporation's fixed-income options four years ago, Trustees decided to move about 10 percent of the Fund's bond holdings to external management. The goal was to broaden the portfolio's overall diversification, reduce volatility and improve consistency in year-to-year results.

Fiscal 1999 was the second full year of external management. Each of the external managers outperformed the in-house portfolio for the fiscal year, and three of them outperformed their benchmark.

The in-house trading desk entered the world of electronic trading this year as TradeWeb was brought on-line, bringing expanded real-time information and execution.

## Down year for domestic fixed income

Following three months of global turmoil, credit fears and liquidity concerns dissipated as the U.S. economy continued its robust growth. Commodity prices bottomed. The Asian economies improved. The stock market rebounded. And the bond market fell sharply as Treasury yields rose. It was a below-average year for domestic fixed income, especially for portfolios with longer duration benchmarks, such as the one managed by the APFC in-house.

The in-house portfolio returned 1.6 percent for the year, compared to 2.54 percent for Alaska Permanent Capital Management, 2.2 percent for Brinson Partners and 4.03 percent for Sanford Bernstein.



## The globalization of the marketplace

It hit home in Alaska - the year of mergers and acquisitions that saw Safeway take over Carrs, Kroger purchasing Fred Meyer, BP Amoco acquiring ARCO, Bankers Trust merging into Deutsche Bank and Exxon buying out Mobil.

This new wave of acquisitions and mergers represents a fundamental change in corporate attitude and structure that's making a global equity structure a reality, say the Fund's managers.

"Corporate actions to improve financial productivity and strategic positioning in a world of heightened global competition remained the most enduring performance driver of fiscal 1999," said Lazard Frères.

A few statistics place the situation in perspective. The companies comprising the S&P 500 on average derive 25 percent of their revenues overseas versus less than 10 percent just a decade ago. Exxon - which owns 22 percent of Prudhoe Bay and the trans-Alaska pipeline - gets 80 percent of its revenues from abroad, as does pharmaceutical producer Upjohn.

Not only are companies selling their products overseas, they are manufacturing them abroad also. Hewlett Packard designs memory boards in Guadalajara, Mexico, GM makes cars in Europe as well as Asia, and GE manufactures light bulbs in Budapest, Hungary.

All this has led to companies that are more financially productive and more competitive in the global market. As Lazard Frères pointed out: "Companies must continue to cut costs and restructure to improve their return on capital in the face of growing global competition."



LG&E building in Louisville, Kentucky

## *Customer satisfaction pays results*

The LG&E Building is the type of institutional-grade real estate investment that pays double-digit returns to the Fund, not just because of its appealing glass and steel appearance but because of its ability to attract and retain high-quality tenants.

The 281,278-square-foot, Class A office tower is located in downtown Louisville, Kentucky, on the southern shore of the Ohio River. The APFC purchased a 40 percent interest in the building in 1991 – two years after its completion – and bought the remaining 60 percent in 1998 at a discount to market value.

Under the management of LaSalle Advisors, the building is more than 97 percent occupied and serves as corporate headquarters for LG&E, the parent company of Kentucky Utilities Co. and Louisville Gas and Electric Co. This Fortune 500 company this year became the first utility ever to win the coveted J.D. Power and Associates Award for Outstanding Residential Customer Satisfaction. The survey compared the top 118 electric utilities nationwide, serving more than 81 million residential customers and 90 percent of the nation's households.

Tenants like LG&E, which occupies 200,000 square feet and continues to grow, help maintain the value of the Fund's direct equity investments. The LG&E Building generated more than \$4 million in net operating income in fiscal 1999. That represents a 14.3 percent return on its current value.

While total return was sub-par, interest income increased 8 percent, totaling \$707 million, an amount equal to oil royalties and severance taxes deposited into the state's general fund.

The APFC's two international bond managers experienced strong results, outperforming their index. Julius Baer ended the year with a 7.34 percent return and Rogge Asset returned 9.65 percent. In recognition of their consistent performance, Trustees expanded their mandate, changed their benchmark and increased their funding. Within specified limits, the two can opportunistically buy a designated percentage of high-grade investments outside the authorized list when they identify opportunities to add value.

### **Changing ownership position**

Three years ago, the Trustees adopted a strategic real estate plan that redefined the composition of the Fund's portfolio. Faced with a collection of minority investments over which the Corporation had little control, staff focused on shifting this portfolio into majority- or wholly-owned direct equity investments. The primary reason for making this change was to increase the Corporation's liquidity in these investments and provide increased control over operating and investment expenses. Thirty-five percent of the portfolio has been redirected into Real Estate Investment Trusts (REITs) and mortgages. Five percent was set aside for other investment opportunities which may arise. The goals are to be invested in a more diversified portfolio with enhanced performance and increased cash flow.

By the end of fiscal 1999, the APFC had implemented the major elements of the plan and had entered into a contract with Lend Lease Real Estate Investors to manage a mortgage portfolio.

As of June 30, 1999, the Fund had \$2.1 billion invested in real estate. The direct equity component has approximately \$1.5 billion invested in 62 properties. The Corporation sold 17 properties during the year, purchased two and increased its ownership in 10. Slightly more than 20 percent of the Fund was invested in REITs and a mortgage program that was started in January 1999. At year end approximately 5 percent was invested in commercial mortgage whole loans and CMBS (Commercial Mortgage-Backed Securities).

The portfolio returned 9.8 percent for the year, two percentage points ahead of its target, and produced \$148 million in income, an increase of 18 percent over fiscal 1998.



550 Corporate Center in San Diego, California

## Real Estate Transactions

(DURING FISCAL YEAR 1999)

### Properties Sold

#### OFFICE

One O'Hare Center • Rosemont, Illinois  
Westwood Place • Los Angeles, California

#### RETAIL

McKinley Mall • Hamburg, New York  
Villa Marina • Marina del Rey, California

#### RESIDENTIAL

Mill Pond & Conifer Creek • Aurora, Colorado  
Brookstone Apartments • Chapel Hill, North Carolina  
Chatham's Mark • Irving, Texas  
Conservatory Apartments • Minnetonka, Minnesota  
Hunt's View Apartments • Greensboro, North Carolina  
Lemay Lake Apartments • Eagan, Minnesota  
Logan's Mark • Irving, Texas  
Park at Wells Branch Apartments • Austin, Texas  
The Springs Apartments • Indianapolis, Indiana  
Williamsburg Apartments • Dallas, Texas  
The Enclave Apartments • Englewood, Colorado  
Huntington of North Dallas • Dallas, Texas  
Tuscany Bay Apartments • Orlando, Florida

### Properties Acquired

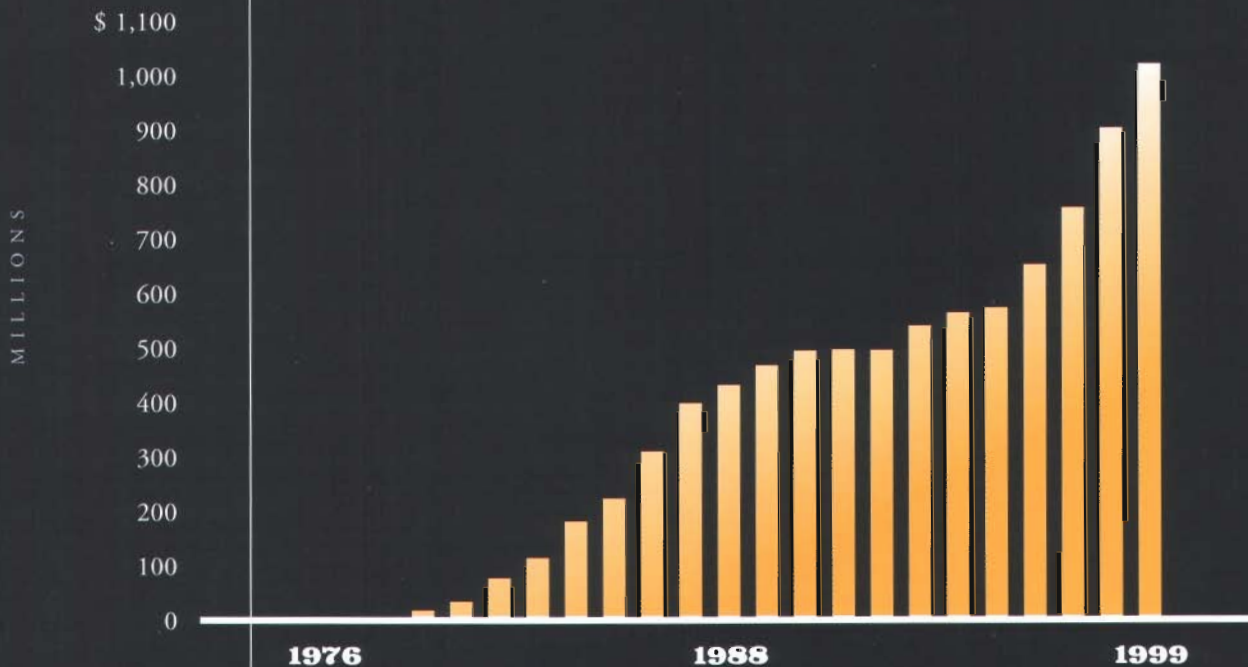
#### OFFICE

One Thomas Circle • District of Columbia  
550 Corporate Center • San Diego, California

### Ownership Increases

	<i>Original Ownership</i>	<i>New Ownership</i>
Aspen Hills Apts. • Smyrna, Georgia	45%	90%
Oakwood Apts. • Orlando, Florida	45%	90%
Polo Club Apts. • Strongsville, Ohio	45%	90%
Preston Village Apts. • Dallas, Texas	45%	90%
Remington Station Apts. • Westerville, Ohio	45%	90%
Sawgrass Apts. • Corpus Christi, Texas	45%	90%
The Wyndham • Hampton, Virginia	45%	90%
Eastridge Apts. • Midvale, Utah	40%	100%
Overlook Apts. • Albuquerque, New Mexico	40%	100%
Royal Farms Apts. • Salt Lake City, Utah	40%	100%

## Income Paid Out for Dividends



# Perma

When Alaskans created the Permanent Fund in 1976, they wanted to save a portion of the North Slope bounty for present and future generations. They succeeded. Today, 58 percent of the Fund's income has been saved for the future and 42 percent – almost \$9 billion – distributed to the current generation through dividends, chart above. While North Slope oil production is less than half what it was a decade ago, oil pumped through the trans-Alaska pipeline, far right, stills flows into the Fund. This year's deposit totaled \$155 million, two-thirds of the \$230 million in fiscal 1998. Just under half of the Fund's principal – \$8.9 billion of \$19 billion – was derived directly from Alaska's oil resources.

*The Fund is a way for all to share in the ownership of state resources, a means to turn a nonrenewable resource into a renewable one.*



## Permanence

It was called a noble experiment by some, a way for all to share in the ownership of state resources, a means to turn a nonrenewable resource into a renewable one.

“The Permanent Fund is an entity created to preserve a portion of the natural resources of Alaska for the permanent benefit of all Alaskans. The income can be used for direct distribution as with the current dividend program or it can be recycled through the political process for public benefit or a combination thereof. The decision is up to the people of Alaska,” said Elmer Rasmuson, the Trustees’ first chairman.

Today, the Fund has grown into Alaska’s largest asset, producing more revenue each year than oil, a total of \$21.3 billion of income since its inception.

“The Permanent Fund was a new concept when it was created and phase one of this experiment has

## *A site worth bookmarking*

Alaskans have long known how to use technology to link themselves to each other and the world. So it should come as no surprise that more Alaskans are hooked into the World Wide Web than any other state in the union.

Some 95,000 Alaska households have Internet access, according to the National Telecommunications and Information Administration, some 7 percent more than New Hampshire, which is ranked number two.

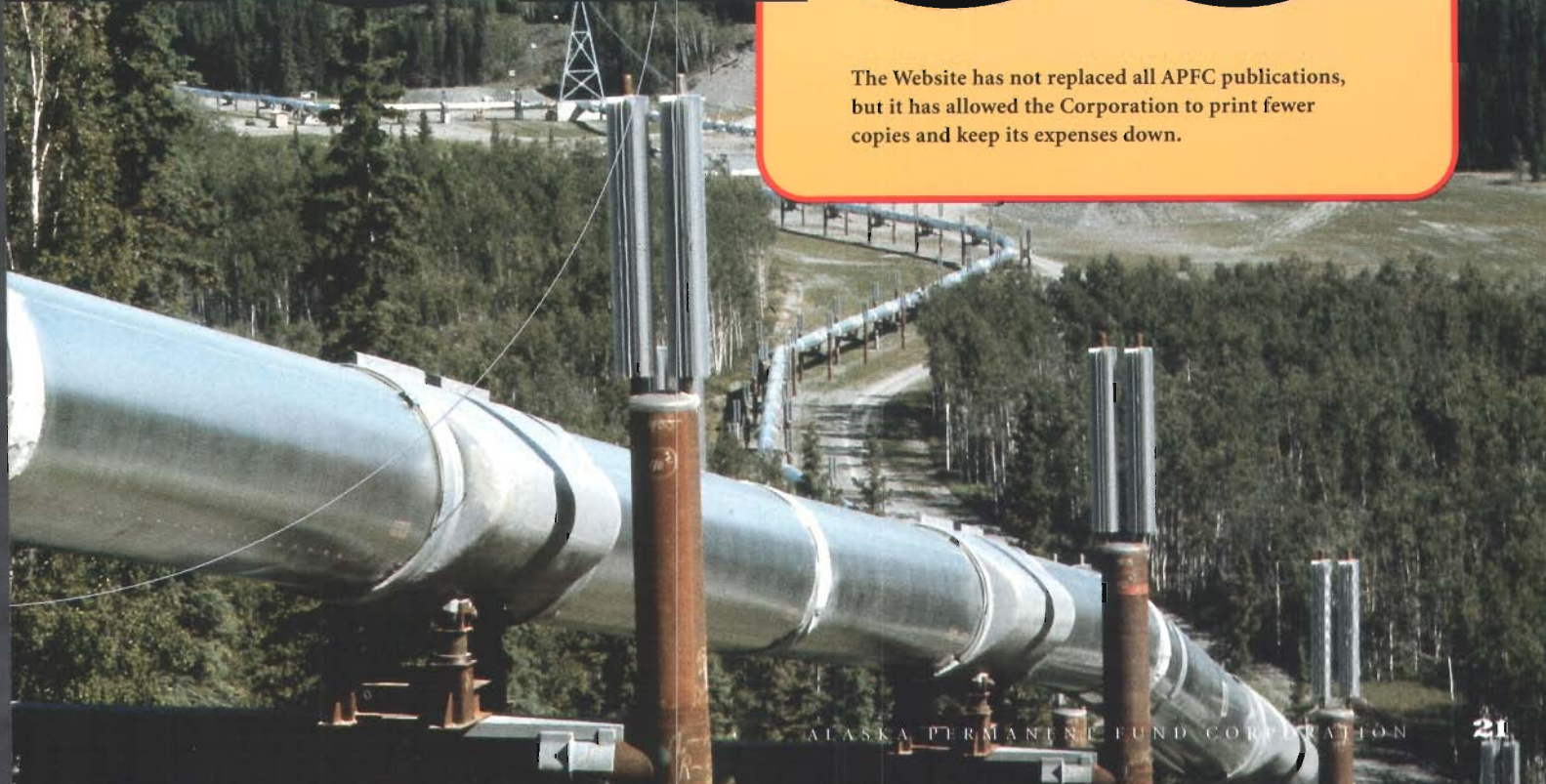
The APFC moved four years ago to tap into this technology, which is available in virtually every corner of the state and most schools and libraries. It established [www.apfc.org](http://www.apfc.org), with the goal of creating a one-stop repository on Fund information and operations that would be easily accessible to all Alaskans. All APFC publications, including annual reports and quarterly financial reports, are posted the same time they’re printed.

The site has grown to more than 200 pages and includes daily position reports on the Fund’s balance and portfolios, performance information on all of the APFC’s external managers and current operating reports. You can browse through Fund history and state law, play a game or two, meet the Trustees and staff or examine details of the Fund’s many investments.

The site is updated daily through administrative interfaces with the APFC’s Management Information System.

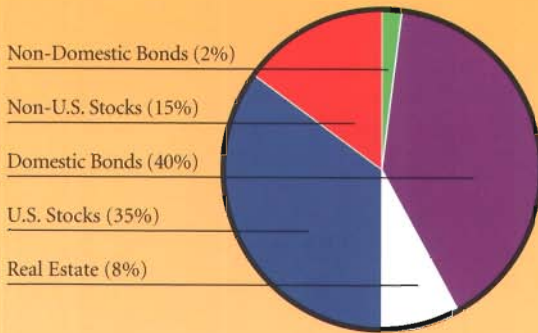
The Website has not replaced all APFC publications, but it has allowed the Corporation to print fewer copies and keep its expenses down.

# Permanence



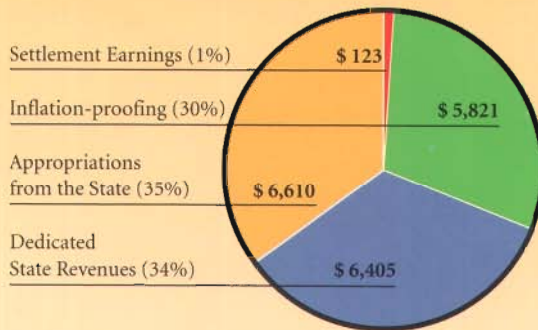
### The Fund's Asset Allocation

(JUNE 30, 1999)



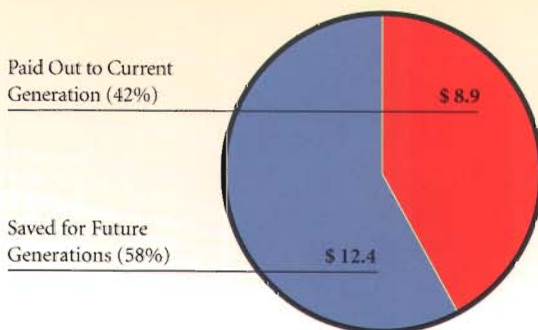
### Sources of Principal

(CUMULATIVE SINCE INCEPTION, IN MILLIONS)



### Uses of Fund Income

(SINCE INCEPTION, IN MILLIONS)



worked exceedingly well,” said Marc Langland, former Trustee and Board Chair. “We have managed to transform a non-renewable asset into a renewable one, with the risk diversified globally.

“Now, as we move into phase two, the true test is whether Alaskans can use this asset in a way that strengthens our state and supports further development and growth.”

### A conservative outlook

The success of the Fund is due in large part to the farsightedness of Alaska’s elected representatives. Left by itself, with its conservative list of investments and its mandate to be a long-term investor, the Fund could never have prospered as it has. Its first Trustees set a long-term goal of a 3 percent real rate of return. Later Trustees increased that to 4 percent. In reality, the inflation-adjusted realized rate of return has been 7.1 percent over the last 15 years.

While legislators at first kept investment risk minimal, they increasingly enlarged the principal through special appropriations and by transferring surplus Fund earnings to the corpus. More than one-third of the principal – \$6.6 billion – comes from state appropriations.

Legislators also fully inflation-proofed the principal so it maintained its real value over the long-term, adding another \$5.8 billion of Fund income to principal.

### Diversification through asset allocation

“By law the Fund is to be managed for the benefit of all generations of Alaskans. So far everything has worked the way it was supposed to. Let’s hope this is the case through the next century,” said Oral E. Freeman, former legislator, former Trustee and Board Chair.

To date, 58 percent of the Fund's \$21.3 billion in earnings have been preserved for the future and \$8.9 billion paid out to the current generation, primarily through dividends. This year's dividend distribution totals \$1.05 billion.

The Fund generates income by investing in stocks, bonds and real estate. Deciding how much to invest in any one type of investment is called asset allocation and is the primary responsibility of the Trustees. It's a simple concept that is deceptively complex, which is why the Trustees spend so much time on it. As former Trustee Rasmuson pointed out 19 years ago, "the top performer in a particular year is due largely to that investment style coming into favor. Top performance carries more risk in terms of volatility and the number one in any year is likely to be the dud in the next. Diversification in style as well as security is essential."

This year the Trustees adopted an asset allocation plan that provides for a target equities allocation of 48 percent with a control band of plus 4 percent and minus 3 percent, a fixed-income allocation of 42 percent with a control band of plus 6 percent and minus 6 percent and a real estate allocation of 10 percent with a plus 2 percent and minus 3 percent.

Within the equities allocation are control bands on style, cap size and location. Bonds have controls on internal and external management. Real estate has controls on direct equity, commingled funds, REITs, mortgages and other investments.

The overall asset allocation is driven by legislative mandate, primarily the ceiling on equities. The control bands serve to deal with short-term imbalances around strategic targets and allow staff tactical flexibility.



*Webbush Morgan Securities participates in the directed brokerage program. From left: Thomas Packer, Matthew Kasper and Sheryl Wagner.*

## *Investing in Alaska*

**The Fund is a working asset that directly impacts the lives of Alaskans through its many outreach programs.**

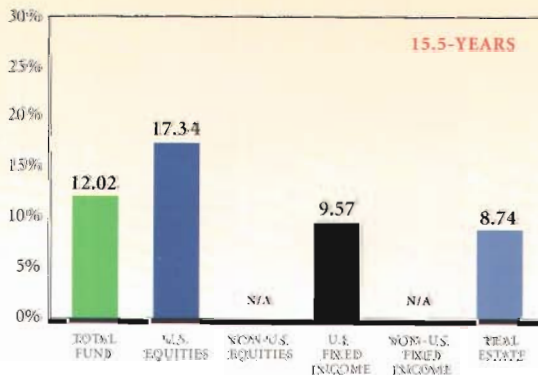
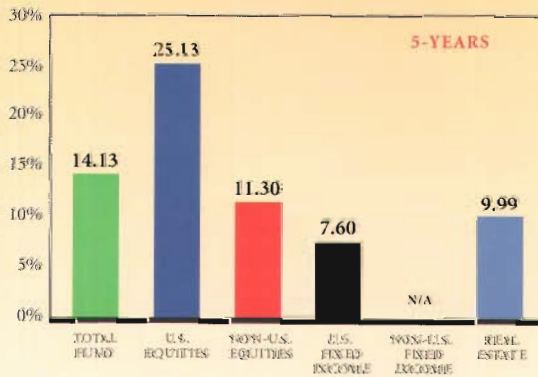
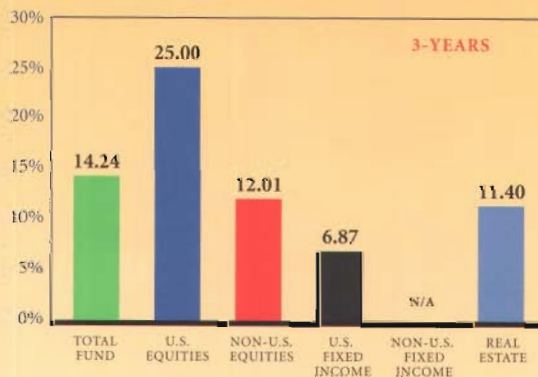
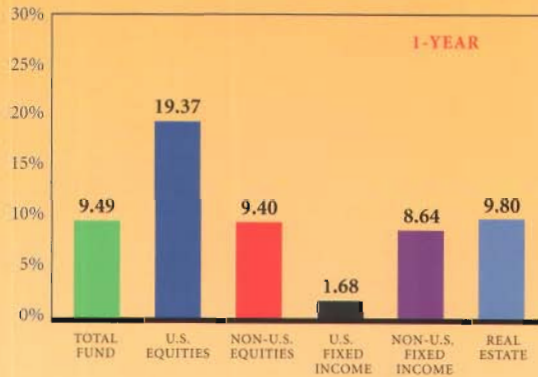
Each year, the APFC helps Alaskans enter the financial world through its internship program. In partnership with the Fund's investment managers, advisors and custodians, the program provides field training opportunities to dozens of Alaska college juniors, seniors and recent graduates. Nearly a quarter of the interns end up with permanent jobs, including Chermaine Fullinck, a University of Alaska Fairbanks student who was hired by Ark Asset Management this year.

The APFC also draws on the expertise of its managers to help other Alaska institutional investors hone their expertise through sponsorship of an annual statewide educational symposium and special workshops at the Corporation's annual meeting. Managers also speak to business organizations throughout the year and appear with APFC staff and Trustees on a statewide, radio call-in program scheduled in conjunction with the annual mid-winter capital market outlook.

The Corporation has established a number of programs for direct investment in the state, including ownership of Alaska real estate properties and Alaska certificates of deposit, which provide capital for state businesses. Its directed brokerage program ensures that Alaska businesses share in commissions generated by the Fund's stock trades. More than \$1 million was returned to in-state brokers this year.

## Average Annual Total Returns

(ALL YEARS ENDING JUNE 30, 1999)



## Prudent investor rule

From the beginning, Fund Trustees have been legislatively bound to follow the prudent investor rule. This mandate, which dates back to the 1800s, requires that the process of investment decisions be documented and that certain criteria be considered before investment decisions are made. Investment decisions must be based on financial returns and safety of the principal that preclude social or political decisions. The prudent investor rule has insulated the Fund from non-investment-grade, in-state investments and political and social investments. The focus has instead been on bottom-line performance.

## Keeping Alaskans involved

The Corporation is required to produce an annual report “in plain English” to keep the Corporation accountable to the citizens of the state. Early on, the APFC decided to involve Alaskans on an ongoing basis, which led to a comprehensive communications effort stressing openness, timeliness and use of technology. In addition, through the *Celebrate Alaska!* program, the APFC’s internship program and other outreach programs, the Corporation attempts to add value to Alaska’s residents in ways that impact individual lives.

## What’s next?

As the Fund enters the next century, Alaskans will continue to debate its purpose and the use of its earnings. That discussion will be supported by a healthy, growing Fund well-positioned to play its role as defined by Alaskans and their elected representatives. As former Trustee and economist George Rogers said, “The good news is that the Fund is still here and safely invested awaiting its use for the purpose originally intended.”

The Board of Trustees  
Alaska Permanent Fund Corporation  
(A Component Unit of the State of Alaska)

We have audited the accompanying statements of assets, liabilities, principal and earnings reserve of the Alaska Permanent Fund (a Component Unit of the State of Alaska) as of June 30, 1999 and 1998, and the related statements of revenues and expenses, changes in principal and earnings reserve, and cash flows for the years then ended. These financial statements are the responsibility of the Alaska Permanent Fund's management. Our responsibility is to express an opinion on these financial statements based on our audits.

We conducted our audits in accordance with generally accepted auditing standards. Those standards require that we plan and perform the audit to obtain reasonable assurance about whether the financial statements are free of material misstatement. An audit includes examining, on a test basis, evidence supporting the amounts and disclosures in the financial statements. An audit also includes assessing the accounting principles used and significant estimates made by management, as well as evaluating the overall financial statement presentation. We believe that our audits provide a reasonable basis for our opinion.

In our opinion, the financial statements referred to above present fairly, in all material respects, the financial position of the Alaska Permanent Fund (a Component Unit of the State of Alaska) as of June 30, 1999 and 1998, and the results of its operations and its cash flows for the years then ended in conformity with generally accepted accounting principles.

The year 2000 supplementary information is not a required part of the financial statements, but is supplementary information required by the Governmental Accounting Standards Board, and we did not audit and do not express an opinion on such information. Further, we were unable to apply to the information certain procedures prescribed by professional standards because of the nature of the subject matter underlying the disclosure requirements and because sufficiently specific criteria regarding the matters to be disclosed have not been established. In addition, we do not provide assurance that the Alaska Permanent Fund is or will become year 2000 compliant, that the Alaska Permanent Fund's year 2000 remediation efforts will be successful in whole or in part, or that parties with which the Alaska Permanent Fund does business are or will become year 2000 compliant.

KPMG LLP

August 13, 1999

## Statements of Assets, Liabilities, Principal and Earnings Reserve

June 30

1999

1998

### Assets

Cash and temporary investments	\$ 361,181,000	507,726,000
Receivables, prepaid expenses and other assets	366,881,000	378,329,000
Investments –		
Marketable debt securities	10,479,125,000	10,595,341,000
Preferred and common stock	13,094,036,000	11,810,661,000
Real estate	2,002,511,000	1,590,966,000
Alaska certificates of deposit	142,415,000	132,452,000
	25,718,087,000	24,129,420,000
Total investments		
<b>TOTAL ASSETS</b>	<b>\$ 26,446,149,000</b>	<b>25,015,475,000</b>

### Liabilities

Accounts payable	\$ 266,046,000	245,955,000
Income distributable to the State of Alaska	1,047,991,000	893,205,000
	1,314,037,000	1,139,160,000
<b>TOTAL LIABILITIES</b>	<b>1,314,037,000</b>	<b>1,139,160,000</b>

### Principal and Earnings Reserve

Principal	18,958,785,000	18,479,031,000
Principal held in escrow	42,124,000	36,945,000
Earnings reserve		
Unrealized earnings reserve	3,540,829,000	3,971,451,000
Remaining earnings reserve	2,590,374,000	1,388,888,000
	6,131,203,000	5,360,339,000
Total earnings reserve		
<b>TOTAL PRINCIPAL AND EARNINGS RESERVE</b>	<b>25,132,112,000</b>	<b>23,876,315,000</b>
<b>TOTAL LIABILITIES, PRINCIPAL AND EARNINGS RESERVE</b>	<b>\$ 26,446,149,000</b>	<b>25,015,475,000</b>

*The accompanying notes are an integral part of the financial statements*

## Statements of Revenues and Expenses

Years Ended June 30

**1999**

**1998**

### Revenues

Investment income –		
Interest	\$ 706,778,000	648,525,000
Dividends	166,892,000	163,557,000
Real estate and other income	153,647,000	126,146,000
<b>TOTAL INVESTMENT INCOME</b>	<b>1,027,317,000</b>	<b>938,228,000</b>
Net increase (decrease) in the fair value of investments –		
Marketable debt securities	(472,196,000)	436,495,000
Preferred and common stock	1,612,041,000	2,064,596,000
Real estate	(10,627,000)	18,290,000
Foreign exchange contracts	18,155,000	12,880,000
Currency	6,609,000	(4,686,000)
<b>TOTAL GAINS</b>	<b>1,153,982,000</b>	<b>2,527,575,000</b>
<b>TOTAL REVENUES</b>	<b>2,181,299,000</b>	<b>3,465,803,000</b>

### Expenses

Operating expenses	(33,529,000)	(30,444,000)
<b>NET INCOME</b>	<b>\$ 2,147,770,000</b>	<b>3,435,359,000</b>
Adjustments to bring net income to statutory net income – settlement earnings and unrealized (gains) losses	396,342,000	(840,522,000)
<b>STATUTORY NET INCOME</b>	<b>\$ 2,544,112,000</b>	<b>2,594,837,000</b>

*The accompanying notes are an integral part of the financial statements*

## Statements of Changes in Principal and Earnings Reserve

Years Ended June 30	1999	1998
<b>Principal</b>		
Balance, beginning of year	\$ 18,479,031,000	17,794,622,000
Dedicated state revenues	155,491,000	230,504,000
Inflation-proofing	288,176,000	422,652,000
Settlement earnings	36,087,000	31,253,000
	<hr/>	<hr/>
BALANCE, END OF YEAR	\$ 18,958,785,000	18,479,031,000
<b>Principal Held in Escrow</b>		
Balance, beginning of year	\$ 36,945,000	32,945,000
Escrow earnings	5,179,000	4,000,000
	<hr/>	<hr/>
BALANCE, END OF YEAR	\$ 42,124,000	36,945,000
<b>Earnings Reserve</b>		
Balance, beginning of year	\$ 5,360,339,000	3,276,090,000
Escrow earnings	(5,179,000)	(4,000,000)
Appropriation to other State Departments	(2,521,000)	(494,000)
Inflation-proofing	(288,176,000)	(422,652,000)
Settlement earnings	(36,087,000)	(31,253,000)
Dividends	(1,044,943,000)	(892,711,000)
Net income	2,147,770,000	3,435,359,000
	<hr/>	<hr/>
BALANCE, END OF YEAR	\$ 6,131,203,000	5,360,339,000
<b>Total</b>		
Balance, beginning of year	\$ 23,876,315,000	21,103,657,000
Dedicated state revenues	155,491,000	230,504,000
Appropriation to the Department of Law	(2,521,000)	(494,000)
Dividends	(1,044,943,000)	(892,711,000)
Net income	2,147,770,000	3,435,359,000
	<hr/>	<hr/>
BALANCE, END OF YEAR	\$ 25,132,112,000	23,876,315,000
<b>Earnings Reserve Breakout</b>		
Provision for escrow earnings	\$ —	5,179,000
Unrealized earnings reserve	3,540,829,000	3,971,451,000
Remaining earnings reserve	2,590,374,000	1,383,709,000
	<hr/>	<hr/>
TOTAL EARNINGS RESERVE	\$ 6,131,203,000	5,360,339,000

The accompanying notes are an integral part of the financial statements

## Statements of Cash Flows

Years Ended June 30

1999

1998

### Cash Flows from Investments

Net (purchases), sales and maturities of investments –		
Marketable debt securities	\$ (403,318,000)	(2,615,847,000)
Preferred and common stock	(1,196,797,000)	(770,770,000)
Real estate	(429,771,000)	(268,112,000)
Alaska certificates of deposit	(9,962,000)	5,758,000
Net change in unsettled trades	23,178,000	271,590,000
Total net (purchases), sales and maturities	(2,016,670,000)	(3,377,381,000)
Investment income received	2,630,480,000	2,611,894,000
Undistributed real estate income	5,639,000	(23,456,000)
NET CASH PROVIDED (USED) BY INVESTMENTS	619,449,000	(788,943,000)

### Cash Flows from Non-capital Financing

Contributions from the State	157,993,000	244,826,000
Income distributions	(892,678,000)	(748,528,000)
NET CASH USED BY NON-CAPITAL FINANCING	(734,685,000)	(503,702,000)

### Cash Flows from Operations

	(31,309,000)	(31,470,000)
Net decrease in cash and temporary investments	(146,545,000)	(1,324,115,000)
Cash and temporary investments at beginning of year	507,726,000	1,831,841,000
CASH AND TEMPORARY INVESTMENTS AT END OF YEAR	\$ 361,181,000	507,726,000

### Reconciliation of Net Income to Net Cash Used by Operations

Net income	\$ 2,147,770,000	3,435,359,000
Adjustments to reconcile net income to net cash used by operations –		
Investment earnings	(2,181,299,000)	(3,465,803,000)
Net change in prepaid expenses and accrued liabilities	2,220,000	(1,026,000)
NET CASH USED BY OPERATIONS	\$ (31,309,000)	(31,470,000)

The accompanying notes are an integral part of the financial statements

## Notes to the Financial Statements

June 30, 1999 and 1998

---

### ENTITY

The Constitution of the State of Alaska (the "State") was amended by public referendum in 1976 to dedicate a portion of certain natural resource revenues to the Alaska Permanent Fund (the "Fund"), a component unit of the State of Alaska. The principal of the Fund is to be invested in perpetuity. The Alaska State Legislature (the "Legislature") created the Alaska Permanent Fund Corporation (the "Corporation"), a government instrumentality of the State that is administered by a board of trustees (the "Trustees"), to manage the investments of the Fund. By statute, (i) a portion of annual earnings is transferred to the State's dividend fund, and (ii) a portion of the earnings reserve account sufficient to offset the impact of inflation is transferred to the principal of the Fund. The balance of earnings is held by the Fund in the earnings reserve account and is subject to appropriation by the Legislature.

The accounting and reporting policies of the Fund conform to generally accepted accounting principles. The Fund follows the accrual method of accounting. In preparing the financial statements, management is required to make estimates and assumptions that affect the reported amounts of assets and liabilities as of the date of the balance sheet and revenue and expenses for the period. Actual results could differ from those estimates. The more significant accounting and reporting policies applied in the preparation of the accompanying financial statements are discussed in the following note.

---

### SIGNIFICANT ACCOUNTING POLICIES

As allowed by the Governmental Accounting Standards Board Statement No. 20, *Accounting and Financial Reporting for Proprietary Funds and Other Governmental Entities That Use Proprietary Fund Accounting*, the Corporation has elected not to apply Statements and Interpretations issued by the Financial Accounting Standards Board after November 30, 1989.

#### CONTRIBUTIONS

Contributions from dedicated state revenues are recorded when certain revenues defined by statute are received or reported by the Alaska Department of Natural Resources. Contributions from appropriations and other sources are recorded when received.

#### DIVIDEND APPROPRIATIONS

Current statutes require that one-half of 21 percent of the Fund's net income for the last five fiscal years, excluding earnings from contributions made in the North Slope royalty case (*State v. Amerada Hess, et al.*), settlements and unrealized gains and losses, be made available for the payment of dividends and other appropriations each year.

#### FORWARD EXCHANGE CONTRACTS

The Fund is party to a variety of forward contracts in its trading activities and in the management of its foreign exchange rate exposure. These contracts are speculative in nature and the contract amounts do not appear on the balance sheet. Realized and unrealized gains and losses are currently included in net income, and are determined on the maturity date of the contracts. Unrealized gains and losses are calculated using foreign currency forward rates at the balance sheet date.

#### INFLATION IMPACT

The impact of inflation is measured by the change in the prior calendar year average of the United States consumer price index for all urban consumers, applied against the balance of contributed equity at the end of the fiscal year. The inflation rates were 1.54 percent and 2.34 percent during the years ended June 30, 1999 and 1998, respectively.

#### INTEREST INCOME

Interest income is accrued monthly as earned.

**INCOME TAXES**

The Internal Revenue Code provides that gross income for tax purposes does not include income accruing to a state or any subdivision thereof, which is derived from the exercise of any essential governmental function. The Fund is a political subdivision of the State performing an essential governmental function and is therefore exempt from federal and state income taxes.

**INVESTMENTS**

The Fund's marketable securities, excluding direct real estate investments, are reported at fair value in the financial statements. Unrealized gains and losses are reported as components of net income. Fair values are obtained from independent sources for marketable debt and equity securities and real estate investment trusts.

Real estate commingled funds, direct real estate investments and direct commercial mortgages are carried at historical cost plus the Fund's share of undistributed earnings. If, in the opinion of management, a permanent impairment of value has occurred, the investment is written down to fair market value by a charge to operations.

The Corporation may invest Fund assets in (i) equity securities up to 55 percent of total Fund investments, and (ii) other investments which meet the test of prudence, including those currently authorized by law, up to 5 percent of total Fund investments.

**SECURITIES TRANSACTIONS**

Securities transactions are recorded on the trade date that securities are purchased or sold.

**STATEMENT OF CASH FLOWS**

The Fund considers all highly liquid short-term investments purchased with a maturity of one year or less to be cash equivalents for purposes of the statement of cash flows.

**CASH AND TEMPORARY INVESTMENTS**

All cash and temporary investments bear interest at competitive rates, and are summarized as follows at June 30:

	<b>1999</b>	<b>1998</b>
Claim on cash (a)	\$ 142,216,000	168,213,000
U.S. agencies (b)	1,393,000	95,239,000
Treasury bills (b)	-	27,937,000
Commercial paper (c)	217,572,000	216,337,000
<b>TOTAL CASH AND TEMPORARY INVESTMENTS</b>	<b>\$ 361,181,000</b>	<b>507,726,000</b>

- a) Share ownership in a money market fund, payable on demand. Collateralized by underlying securities held by the Fund in the name of the custodian. Not considered an investment nor assigned a specific risk category.
- b) Debt obligation guaranteed by the U.S. government.
- c) Commercial paper rated investment grade.

## Notes to the Financial Statements

### RECEIVABLES, PREPAID EXPENSES AND OTHER ASSETS

Receivables, prepaid expenses and other assets at June 30, are as follows:

	<b>1999</b>	<b>1998</b>
Interest receivable	\$ 171,810,000	176,463,000
Dividends receivable	14,221,000	21,491,000
Sales receivable	152,680,000	155,758,000
Foreign exchange contracts	6,786,000	729,000
Contributions receivable	21,384,000	23,886,000
Prepaid expenses	-	2,000
<b>TOTAL RECEIVABLES, PREPAID EXPENSES AND OTHER ASSETS</b>	<b>\$ 366,881,000</b>	<b>378,329,000</b>

### MARKETABLE DEBT SECURITIES

The Corporation is authorized by statute to invest Fund assets in (i) corporate bonds rated investment grade; (ii) obligations of the United States Treasury, its agencies and instrumentalities; and (iii) foreign obligations of comparable quality. All marketable debt securities are held by custodian banks in the name of the Corporation on behalf of the Fund.

Marketable debt securities at June 30 are summarized as follows:

	COST	MARKET	UNREALIZED GAINS/(LOSSES)
<b>1999</b>			
Treasury notes/bonds	\$ 4,366,922,000	4,278,235,000	(88,687,000)
Mortgage-backed securities	795,587,000	790,671,000	(4,916,000)
Other federal agencies	1,315,035,000	1,306,731,000	(8,304,000)
Corporate bonds	3,690,793,000	3,618,564,000	(72,229,000)
Non-domestic bonds	512,488,000	484,924,000	(27,564,000)
<b>TOTAL MARKETABLE DEBT SECURITIES</b>	<b>\$ 10,680,825,000</b>	<b>10,479,125,000</b>	<b>(201,700,000)</b>
<b>1998</b>			
Treasury notes/bonds	\$ 5,011,511,000	5,208,205,000	196,694,000
Mortgage-backed securities	494,775,000	493,972,000	(803,000)
Other federal agencies	1,401,941,000	1,418,739,000	16,798,000
Corporate bonds	2,989,350,000	3,084,841,000	95,491,000
Non-domestic bonds	379,930,000	389,584,000	9,654,000
<b>TOTAL MARKETABLE DEBT SECURITIES</b>	<b>\$ 10,277,507,000</b>	<b>10,595,341,000</b>	<b>317,834,000</b>

**PREFERRED AND COMMON STOCK**

The Corporation is authorized by statute to invest Fund assets in the preferred and common stock of United States and non-domestic corporations. All preferred and common stock investments are held by custodial banks in the name of the Corporation on behalf of the Fund.

Preferred and common stock at June 30 are summarized as follows:

	COST	MARKET	UNREALIZED GAINS/(LOSSES)
<b>1999</b>			
Domestic	\$ 6,351,224,000	9,430,628,000	3,079,404,000
Non-domestic	2,998,677,000	3,663,408,000	664,731,000
<b>TOTAL PREFERRED AND COMMON STOCK</b>	<b>\$ 9,349,901,000</b>	<b>13,094,036,000</b>	<b>3,744,135,000</b>
<b>1998</b>			
Domestic	\$ 5,968,362,000	9,097,809,000	3,129,447,000
Non-domestic	2,184,742,000	2,712,852,000	528,110,000
<b>TOTAL PREFERRED AND COMMON STOCK</b>	<b>\$ 8,153,104,000</b>	<b>11,810,661,000</b>	<b>3,657,557,000</b>

**REQUIRED SUPPLEMENTARY INFORMATION - UNAUDITED**

Some of the Corporation's older computer systems identify years with two digits instead of four, which may cause these systems to recognize the year 2000 as the year 1900. These problems could result in a system failure or miscalculations that disrupt operations, including a temporary inability to process transactions, receive and process financial data, process payments or engage in similar, normal business activities. In addition, the Corporation faces the risk that suppliers of data, services and systems do not comply with the year 2000 requirements.

While management believes the conversions or installations of replacement systems by the Corporation will proceed smoothly, unforeseen interruption or failures in our systems or in the systems of our vendors may occur.

To understand the Corporation's vulnerability to the year 2000 issue, management conducted a complete systems assessment of year 2000 compliance. Many systems have been represented by their respective vendors to be year 2000 compliant, and the Corporation has initiatives in progress that we believe will address all outstanding year 2000 issues. The Corporation has currently remediated 90 percent of its systems and is in the process of validating and testing changes made during the conversion process.

Since January 1, 1997, the Corporation has spent approximately \$2 million to upgrade and maintain its information technology systems. While each of these upgrades relates to systems that, based on representations by the vendors, management believes are year 2000 compliant, the expenditures for upgrading these systems also include costs of replacing otherwise obsolete systems. The Corporation expects to spend an additional \$200,000 to make the information technology systems year 2000 compliant by the end of the third quarter of 1999.

Given the progress made to date, we do not anticipate delays in finalizing and implementing year 2000 readiness solutions. The Corporation cannot accurately estimate the uncertainty of completing the year 2000 readiness plan, particularly as it relates to any failure by third parties that have material relationships with us and fail to achieve their own year 2000 readiness. Any failures by these third parties to appropriately address their own year 2000 readiness challenges could affect our financial condition; however, management believes that the Corporation's contingency planning will minimize such impacts.

## Notes to the Financial Statements

### REAL ESTATE

The Corporation is authorized by statute to invest Fund assets in real estate improved by substantially rented buildings located in the United States. Real estate investments may take the form of equity interests, real estate title-holding entities, investment trusts, operating companies or other entities whose assets consist primarily of real property, debt obligations secured by real property or similar entities. All real estate investments are held by the Corporation in its own name on behalf of the Fund, and are managed by professional real estate management firms.

The carrying value of real estate at June 30 was \$2,002,511,000 in 1999 and \$1,590,966,000 in 1998. Carrying value consists of the equity value of direct real estate investments, commingled funds and commercial mortgages and the market value of real estate investment trusts and commercial mortgage backed securities.

Real estate investments at June 30 are summarized as follows:

	BOOK VALUE	MARKET	UNREALIZED GAINS/(LOSSES)
<b>1999</b>			
Commingled funds	\$ 16,845,000	20,346,000	3,501,000
Real estate investment trusts	470,599,000	462,338,000	(8,261,000)
Commercial mortgages	11,646,000	11,646,000	-
Commercial mortgage-backed securities	112,608,000	112,269,000	(339,000)
Alaska residential mortgages	207,000	207,000	-
Direct investments –			
Retail	333,819,000	353,324,000	19,505,000
Office	581,964,000	659,703,000	77,739,000
Industrial	158,034,000	167,049,000	9,015,000
Residential	325,389,000	349,188,000	23,799,000
<b>TOTAL REAL ESTATE</b>	<b>\$ 2,011,111,000</b>	<b>2,136,070,000</b>	<b>124,959,000</b>
<b>1998</b>			
Commingled funds	\$ 36,006,000	34,845,000	(1,161,000)
Real estate investment trusts	273,162,000	277,148,000	3,986,000
Alaska residential mortgages	216,000	216,000	-
Direct investments –			
Retail	369,337,000	395,513,000	26,176,000
Office	449,589,000	449,591,000	2,000
Industrial	169,368,000	179,298,000	9,930,000
Residential	289,302,000	314,461,000	25,159,000
<b>TOTAL REAL ESTATE</b>	<b>\$ 1,586,980,000</b>	<b>1,651,072,000</b>	<b>64,092,000</b>

**Summary of APFC's Real Estate Investments**

**INDUSTRIAL PROPERTIES**

MIW-OPUS Properties .....	<i>Indianapolis, Indiana</i>
Eastpoint Associates .....	<i>Dallas, Texas</i>
Dallas Industrial .....	<i>Dallas, Texas</i>
Northgate Business Park .....	<i>Garland, Texas</i>
Southgate Business Park .....	<i>Lanham, Maryland</i>
Sand Lake West .....	<i>Orlando, Florida</i>
Memphis Industrial .....	<i>Memphis, Tennessee</i>

**OFFICE PROPERTIES**

1010 Arapaho .....	<i>Richardson, Texas</i>
Ericsson Counterpoint .....	<i>Richardson, Texas</i>
1701 K Street .....	<i>Washington, D.C.</i>
Frontier Building .....	<i>Anchorage</i>
International Place .....	<i>Richardson, Texas</i>
Goldbelt Building .....	<i>Juneau</i>
770 L Street .....	<i>Sacramento, California</i>
919 North Michigan .....	<i>Chicago, Illinois</i>
Arboretum Lakes .....	<i>Lisle, Illinois</i>
580 Walnut Building .....	<i>Cincinnati, Ohio</i>
ARAMARK Tower .....	<i>Philadelphia, Pennsylvania</i>
LG&E Building .....	<i>Louisville, Kentucky</i>
Providence Towers .....	<i>Dallas, Texas</i>
One Thomas Circle .....	<i>Washington, D.C.</i>
4111 Northside Parkway .....	<i>Atlanta, Georgia</i>
Parkway Center .....	<i>Marietta, Georgia</i>
550 Corporate Center .....	<i>San Diego, California</i>
Tower Center II .....	<i>East Brunswick, New Jersey</i>
Warner Center Properties .....	<i>Woodland Hills, California</i>

**RESIDENTIAL PROPERTIES**

Island Club Apartments .....	<i>Miami, Florida</i>
Ontario Place .....	<i>Chicago, Illinois</i>
Aspen Hills Apartments .....	<i>Smyrna, Georgia</i>
Oakwood Apartments .....	<i>Orlando, Florida</i>
Polo Club Apartments .....	<i>Strongsville, Ohio</i>
Preston Village Apts. ....	<i>Dallas, Texas</i>
Remington Station Apts. ....	<i>Westerville, Ohio</i>
Sawgrass Apartments .....	<i>Corpus Christi, Texas</i>
The Wyndham .....	<i>Hampton, Virginia</i>
Bent Tree Apartments .....	<i>Centerville, Virginia</i>
Lexington & Mariner's .....	<i>Raleigh, North Carolina</i>
Avalon Park Apartments .....	<i>Tigard, Oregon</i>
Bristol Place Apartments .....	<i>Tampa, Florida</i>
Crystal Creek Apartments .....	<i>Henderson, Nevada</i>

Eastridge Apartments .....	<i>Midvale, Utah</i>
Innesbrook Apartments .....	<i>Durham, North Carolina</i>
Lakefront Apartments .....	<i>Orlando, Florida</i>
Overlook Apartments .....	<i>Albuquerque, New Mexico</i>
Royal Farms Apartments .....	<i>Salt Lake City, Utah</i>
Skyler Ridge Apartments .....	<i>Overland Park, Kansas</i>
Zia Vista Apartments .....	<i>Santa Fe, New Mexico</i>
Bridgewater Apartments .....	<i>St. Petersburg, Florida</i>
Colonnade at Willow Bend .....	<i>Plano, Texas</i>
Tree Tops Apartments .....	<i>West Chester, Pennsylvania</i>

**RETAIL PROPERTIES**

Plaza Port West .....	<i>Ketchikan</i>
Oakwood Mall .....	<i>Enid, Oklahoma</i>
Builder's Square II .....	<i>Houston, Texas</i>
Danada Centers .....	<i>Wheaton, Illinois</i>
Orland Towne Center .....	<i>Orland Hills, Illinois</i>
Darien Towne Center .....	<i>Darien, Illinois</i>
Galleria at Southpointe .....	<i>Mt. Lebanon, Pennsylvania</i>
Monroeville Mall .....	<i>Monroeville, Pennsylvania</i>
Fiesta Mall .....	<i>Mesa, Arizona</i>
120 East 87th Street .....	<i>New York, New York</i>
Commons at Willowbrook .....	<i>Houston, Texas</i>
Tyson's Corner Center .....	<i>McLean, Virginia</i>

**POOL PROPERTIES**

JMB II .....	<i>Nationwide</i>
Aetna Fund I .....	<i>Nationwide</i>
Cigna Fund S .....	<i>Nationwide</i>
JMB III .....	<i>Nationwide</i>

**OTHER**

REITs .....	<i>Nationwide</i>
Commercial Mortgages .....	<i>Nationwide</i>

**TYPES OF APFC REAL ESTATE HOLDINGS**

<i>(as of June 30, 1999)</i>	PERCENT OF PORTFOLIO
Residential	16%
Industrial	8
Office	29
Retail	17
Commingled Funds	1
REITs Public	21
REITs Private	2
Mortgages	6

## Notes to the Financial Statements

### ALASKA CERTIFICATES OF DEPOSIT

The Corporation is authorized by statute to invest Fund assets in certificates of deposit or the equivalent instruments of banks, savings and loan associations, mutual savings banks and credit unions doing business in Alaska. Letters of credit from the Federal Home Loan Bank secure these investments. The market value of these certificates approximates cost.

### ACCOUNTS PAYABLE

Accounts payable at June 30 are summarized as follows:

	<u>1999</u>	<u>1998</u>
Accrued liabilities	\$ 10,030,000	7,812,000
Service fees payable	1,753,000	1,714,000
Foreign exchange contracts payable	-	2,266,000
Securities purchased	234,263,000	234,163,000
<b>TOTAL ACCOUNTS PAYABLE</b>	<b>\$ 266,046,000</b>	<b>245,955,000</b>

### INCOME DISTRIBUTABLE TO THE STATE OF ALASKA

The Legislature appropriated a portion of the Fund's net income for various purposes, including the payment of dividends to qualified residents of the State of Alaska. In addition, the Legislature appropriated a portion of the Fund's earnings reserves for the cost of oil and gas revenue litigation. Income distributable to the State at June 30 is summarized as follows:

	<u>1999</u>	<u>1998</u>
Dividends	\$ 1,016,113,000	863,982,000
Appropriation to the Departments of -		
Corrections	2,147,000	1,047,000
Health and Social Services	18,689,000	19,101,000
Revenue	4,793,000	5,677,000
Public Safety	3,234,000	2,904,000
Total to Dividend Fund	1,644,976,000	892,711,000
Other Departments	3,015,000	494,000
<b>TOTAL INCOME DISTRIBUTABLE</b>	<b>\$ 1,047,991,000</b>	<b>893,205,000</b>

**PRINCIPAL**

The principal balance of the Fund at June 30 is shown in Table I.

The Fund received dedicated State revenues from North Slope royalty case (*State v. Amerada Hess, et al.*) settlements. By statute, earnings from these settlements are to be treated in the same manner as other Fund income, except that earnings on settlements are excluded from the dividend calculation. Accumulated settlement-related activity which is included in the principal balance of the Fund at June 30 is shown in Table II. Total earnings on settlement principal were \$41,188,000 in 1999 and \$38,107,000 in 1998. Of these amounts, \$5,102,000 and \$6,853,000 during 1999 and 1998 respectively, were added to inflation-proofing. The remaining earnings of \$36,086,000 and \$31,254,000 during 1999 and 1998 respectively, have been added to Fund principal in accordance with law.

**Table I**

	<b>1999</b>	<b>1998</b>
Dedicated state revenues	\$ 6,405,164,000	6,249,672,000
Appropriations from the state	6,609,555,000	6,609,555,000
Inflation-proofing	5,820,502,000	5,532,326,000
Settlement earnings	123,564,000	87,478,000
<b>TOTAL PRINCIPAL</b>	<b>\$ 18,958,785,000</b>	<b>18,479,031,000</b>

**Table II**

	<b>1999</b>	<b>1998</b>
Settlement –		
Principal	\$ 208,769,000	208,769,000
Earnings	123,564,000	87,478,000
Inflation-proofing	40,098,000	34,996,000
<b>TOTAL SETTLEMENT PRINCIPAL</b>	<b>\$ 372,431,000</b>	<b>331,243,000</b>

**PRINCIPAL HELD IN ESCROW**

In June 1997, the Supreme Court of the United States awarded ownership of all disputed tracts from the joint State-Federal Beaufort Sea lease sale of 1979 to the federal government. The State has asked the Supreme Court to reconsider its decision and the State is negotiating with the federal government on re-defining the boundaries of some of the tracts. As of June 1999, the Supreme Court had not reconsidered its original decision. The Corporation will transfer the balance of principal held in escrow (including associated earnings), to the principal of the Fund on July 1, 1999. Escrow earnings for 1999 will not be transferred as the original escrow amount is now considered regular principal.

## Notes to the Financial Statements

### INVESTMENT INCOME BY SOURCE

Investment income during the years ended June 30 is summarized as follows:

	1999	1998
<b>Interest</b>		
Marketable debt securities	\$ 691,357,000	637,382,000
Alaska certificates of deposit	8,046,000	7,205,000
Cash and other interest	7,375,000	3,938,000
<b>TOTAL INTEREST</b>	<b>\$ 706,778,000</b>	<b>648,525,000</b>
<b>Dividends</b>		
Domestic preferred and common stock	\$ 110,895,000	116,696,000
Non-domestic preferred and common stock	55,997,000	46,861,000
<b>TOTAL DIVIDENDS</b>	<b>\$ 166,892,000</b>	<b>163,557,000</b>
<b>Real Estate and Other Income</b>		
Real estate interest	\$ 6,542,000	5,184,000
Real estate dividends	21,660,000	5,489,000
Other real estate income	119,199,000	113,459,000
Loaned security and other income	6,246,000	2,014,000
<b>TOTAL REAL ESTATE AND OTHER INCOME</b>	<b>\$ 153,647,000</b>	<b>126,146,000</b>

Under Alaska Statute 37.13.120(f), the Corporation is authorized to enter into securities lending transactions. The Corporation lends marketable debt securities to security dealers with substantial capitalization and charges a fee to the borrowers at the prevailing market rate. Such loans have fixed maturity dates with an average life of 30 days and are fully collateralized with similar securities to those on loan, including similar maturity dates. Collateral is held by a custodian bank in the name of the Corporation on behalf of the Fund and is required to be not less than 102 percent of the market value of the loaned securities and accrued interest. The Corporation has the ability to sell collateral securities only after the borrower's defaults. At June 30, 1999, there were \$734 million in loaned securities outstanding. During the years ended June 30, 1999 and 1998, there were no losses incurred as a result of securities lending transactions.

**NET REALIZED GAINS (LOSSES) ON CURRENCY**

Net realized gains and losses on foreign currency for the years ended June 30 consisted of the following elements:

	<b>1999</b>	<b>1998</b>
Security purchases and sales	\$ 3,857,000	46,000
Dividends	-	2,000
Currency inventory	2,752,000	(4,734,000)
<b>GAINS/(LOSSES) ON CURRENCY</b>	<b>\$ 6,609,000</b>	<b>(4,686,000)</b>

**FOREIGN EXCHANGE CONTRACTS AND OFF-BALANCE SHEET RISK**

The Corporation entered into foreign currency forward exchange contracts to buy and sell specified amounts of foreign currencies at specified rates on specified future dates for the purpose of hedging existing cash positions in these currencies. The maturity periods for these contracts ranged from one to five months. At June 30, 1999, the Corporation had net unrealized gains with respect to such contracts.

The counterparties to the foreign currency forward contracts consisted of a diversified group of financial institutions. The Corporation is exposed to credit risk to the extent of non-performance by these counterparties; however, the Corporation considers the risk of default to be remote. The Corporation's market risk is limited to the difference between contractual rates and forward rates at the end of the fiscal year.

At June 30, 1999, the Corporation had net sale contracts outstanding totaling \$568,507,000. The market value of these contracts, using the forward rate at June 30, 1999, was \$561,598,000, resulting in net unrealized gains of \$8,469,000 for the year ended June 30, 1999, including prior year reversals. The Fund had realized gains amounting to \$9,686,000 for the year ended June 30, 1999.

**OPERATING EXPENSES**

Operating expenses of the Corporation for the years ended June 30 are summarized as follows:

	<b>1999</b>	<b>1998</b>
Salaries and benefits	\$ 2,489,000	2,432,000
Travel	257,000	249,000
Communications	866,000	884,000
Custody and safekeeping fees	1,450,000	1,970,000
Consulting fees	364,000	362,000
Investment management fees	23,704,000	22,486,000
Legal and audit fees	356,000	182,000
Public information and subscriptions	374,000	314,000
Rent	495,000	259,000
Property and equipment	559,000	430,000
Other expenses	615,000	876,000
<b>TOTAL OPERATING EXPENSES</b>	<b>\$ 33,529,000</b>	<b>30,444,000</b>

### PENSION PLAN

All full-time employees of the Corporation participate in the State of Alaska Public Employees Retirement System (PERS), a multiple employer public employee retirement system. Total salaries and benefits for employees covered by PERS for the years ended June 30, 1999 and 1998 amounted to \$2,489,000 and \$2,432,000, respectively.

Corporation employees are required to contribute 6.13 percent of their annual salaries to PERS. The Corporation contributes the remaining amounts necessary to pay benefits when due. These contributions represented 8.51 percent and 9.32 percent of covered salary expenses in the years ended June 30, 1999 and 1998, respectively.

### INVESTMENTS MANAGED ON BEHALF OF OTHER ENTITIES

By statute, the Alaska Science and Technology Endowment Fund, the Alaska Mental Health Trust Fund and the International Trade and Business Endowment Fund (other funds) are invested by the Corporation under the same investment authority as the Fund is managed. The assets of the other funds are commingled with the assets of the Fund for investment purposes. Earnings are separately allocated to the other funds on the basis of unit and fractional unit shares, which have undivided beneficial interests in the commingled assets equal to the proportion that such shares bear to the total units outstanding. Unit shares are credited to the other funds on the basis of amounts contributed to the investment pool. The following represents the other funds' shares of the commingled assets, which are not reflected in the accompanying financial statements:

	1999	1998
Alaska Science and Technology Endowment Fund	\$ 124,887,000	129,092,000
Alaska Mental Health Trust Fund	305,939,000	299,356,000
International Trade and Business Endowment Fund	5,927,000	5,710,000
	\$ 436,753,000	434,158,000

### SUBSEQUENT EVENTS

#### SECURITIES LOANS

In August 1999, the Corporation entered a contractual agreement with the Bank of New York (the "Bank") to lend marketable debt and equity securities as agent for the Corporation on its behalf. Collateral may be in the form of securities similar to those on loan or cash, at the option of the borrower. Cash collateral is invested by the Bank and a rebate of income is paid to the borrower. The Bank is compensated with 25 percent of the securities lending income. The Bank charges a securities lending fee on behalf of the Corporation, and U.S. loans are collateralized at 102 percent of market value while non-U.S. loans are collateralized at 105 percent of market value. The Corporation retains the right to sell securities on loan. The Bank may sell collateral upon borrower default.

This publication on the activities and financial condition of the Alaska Permanent Fund Corporation is submitted in accordance to AS 44.88.210. This report was printed at a cost of \$2.98 per copy on recycled paper in Anchorage, Alaska.

## **Executive Staff**

**Byron I. Mallott**  
*Executive Director and  
Corporate Secretary/Treasurer*

**Sandra Firestack**  
*Executive Assistant*

## **Investments Staff**

**Terry A. Brown**  
*Chief Investment Officer*

**Randy Sears**  
*Manager of Fixed-Income Investments*

**Richard D. Shafer**  
*Senior Investment Officer  
Fixed Income*

**Michael T. Bell**  
*Investment Officer  
Equities*

**Steven J. Eason**  
*Investment Officer  
Fixed Income*

**Peter M. Naoroz**  
*Manager of Real Estate Investments*

**Christi Grussendorf**  
*Investment Officer  
Real Estate*

**Andrew Donovan**  
*Investment Officer  
Real Estate*

**Paul Hanson**  
*Investment Associate*

**Joyce Andrews**  
*Investments Executive Secretary*

## **Administration Staff**

**Patricia Belec**  
*Director of Administration*

**Freda Westman**  
*Administrative Officer*

**Kathy L. Thatcher**  
*Administrative Specialist*

**Bob Baxter**  
*Procurement Specialist*

**Shawn Lew**  
*Administration Executive Secretary*

**Anna Jacobson**  
*Receptionist/Secretary*

## **Finance Staff**

**Peter A. Bushre**  
*Chief Financial Officer*

**Calvin Kubota**  
*Controller*

**Rosemarie Santana**  
*Senior Portfolio Accountant*

**Valerie Mertz**  
*Portfolio Accountant*

**Tobie Putman**  
*Accountant*

**Karen Emberton**  
*Accounting Technician*

**David W. Riccio**  
*Information Technology Manager*

**William Johnson**  
*Senior Information Technology Specialist*

**Robert McKnight**  
*Information Technology Specialist*

**Dan Hendrix**  
*Information Technology Specialist*

**Maryantonia L. Kensinger**  
*Finance Executive Secretary*

## **Communications Staff**

**Jim Kelly**  
*Director of Communications*

**Joan Cahill**  
*Communications Assistant*

## MAILING ADDRESS

P.O. Box 25500  
Juneau, Alaska 99802-5500

## PHYSICAL ADDRESS

801 West 10th Street  
Suite 302  
Juneau, Alaska 99801

## TELEPHONE

(907) 465-2047

## FAX

(907) 586-2057

## TTY/TDD

(907) 465-4355

## WEBSITE

[www.apfc.org](http://www.apfc.org)

Design by Northwest Strategies.  
Printing by Professional Color  
Graphics. Cover photograph by  
Calvin W. Hall.



**Alaska Permanent Fund Corporation**

---

801 W. 10th Street, Suite 302, Juneau, Alaska 99801 • [www.apfc.org](http://www.apfc.org)